Jurisdictional Statement

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No. ....

IN THE

Supreme Court of the United States

October Term, 1981

GLENDALE FEDERAL SAVINGS AND LOAN ASSOCIATION and VERDUGO SERVICE CORPORATION,

Appellants,

vs.

DEAN L. GROSS and PEDRO ENRIQUEZ,

Appellees.

On Appeal From the Court of Appeal of the State of California, Fourth Appellate District, Division Two.

JURISDICTIONAL STATEMENT

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Question Presented.

An act of the United States Congress, the Home Owners' Loan Act of 1933, 12 U.S.C. §1464 *et seq.* ("HOLA"), states that a federal agency, the Federal Home Loan Bank Board ("the Bank Board"), "is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation" of federally chartered savings and loan associations. Pursuant to that statute, the Bank Board has promulgated a regulation, now 12 C.F.R. §545.8-3(f) and (g), expressly confirming (subject to certain restrictions not here relevant) the authority of a federally chartered savings and loan association to include in its mortgage loan contracts and "automatically" exercise according to its terms a provision, commonly known as a "due-on-sale" clause, permitting the association to declare the unpaid principal balance of a loan immediately due and payable in the event that the borrower transfers or conveys the real property hypothecated as security for the loan ("the federal 'due-on-sale' regulation").

A California statute, California Civil Code §711, as interpreted by the California Supreme Court in *Wellenkamp v. Bank of America,* 21 Cal.3d 943, 582 P.2d 970, 148 Cal.Rptr. 379 (1978), proscribes the "automatic" exercise of a "due-on-sale" clause as an unlawful restraint on alienation.

Accordingly, the question presented by the within appeal is whether HOLA and 12 C.F.R. §545.8-3(f) and (g) preempt state laws such as California Civil Code §711 with respect to the "due-on-sale" practices of federally chartered savings and loan associations.*

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*In the opinion from which the within appeal is taken, the Court of Appeal for the State of California, Fourth Appellate District, Division Two (sometimes, "the Court of Appeal"), recited that its decision regarding the question presented was "comprehensively treated and

(footnote continued on following page)

Parties to the Appeal.

The Appellants in the within appeal are Glendale Federal Savings and Loan Association and Verdugo Service Corporation.** The Appellees are Dean L. Gross and Pedro Enriquez.

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disposed of" in its decision in *de la Cuesta v. Fidelity Federal Savings & Loan Association*, 121 Cal.App.3d 328, 175 Cal.Rptr. 467, *appeal docketed*, No. 81-750 (U.S. 1981). The mortgage loan contract involved in *de la Cuesta*, however, provided, in pertinent part, that "[t]his Deed of Trust shall be governed by the law of the jurisdiction in which the property is located", whereas no such provision is contained in the mortgage loan contract that is involved in the within appeal. *Hence the within appeal, unlike an appeal to this Court from the decision in de la Cuesta, does not involve any issue arising out of the presence in the mortgage loan contract of a "law of the jurisdiction" clause.* (See footnote 1, *infra*.)

**Pursuant to Rule 28.1 of the Supreme Court Rules, the subsidiaries and/or affiliates of Glendale Federal Savings and Loan Association and Verdugo Service Corporation include the following: (1) Wilshire Glen Services, Inc.; (2) Wilshire Mortgage Corporation; (3) Wilshire Diversified, Inc.; (4) Verdugo Builders, Inc., dba Pacific Glen Insurance Agency; (5) San Juan Hills Country Club; (6) Fir-Fed Services Corporation; (7) Wilshire Realty Investments; (8) Outlook Development Corporation; (9) Hampton Homes and Housing Corporation, dba Florida Communities Oceanside; (10) Sentinel Communities, Inc., dba Florida Communities and the Woodhawk Club; (11) Sentinel Broward, Inc., dba Florida Communities of Broward; (12) Sentinel Highland, Inc., dba Florida Community Highland Beach and Hidden Harbor Club; (13) Hutchinson Island Homes, Inc., dba Florida Communities Hutchinson Island; (14) Horizons Development, Inc., dba Rolling Hills Lake Estates; (15) Oceanside Communities, Inc., dba Sea Ranch Club of Boca and Bonaventure Joint Venture; (16) Boca Coast Communities, Inc., dba Sea Ranch of Boca Intracoastal; (17) Florida Southern Mortgage Corporation; and (18) Florida Real Estate Appraisers, Inc.

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IN THE

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GLENDALE FEDERAL SAVINGS AND LOAN ASSOCIATION and VERDUGO SERVICE CORPORATION,

Appellants,

vs.

DEAN L. GROSS and PEDRO ENRIQUEZ,

Appellees.

JURISDICTIONAL STATEMENT

I.
OPINION BELOW.

The opinion of the Court of Appeal from which the within appeal is taken, a copy of which is attached hereto at Appendix, pp. 1-4, has not been published in any official report or, to the best of Appellants' knowledge, in any unofficial report.[1]

[1]Also reproduced at Appendix, pp. 5-30, is a copy of the decision of the Court of Appeal in *de la Cuesta v. Fidelity Federal Savings & Loan Association, supra,* from which an appeal to this Court is also currently pending. Nevertheless, and although the central issue in both cases is the same, the appeal to this Court from the *de la Cuesta* decision and the appeal to this Court in the within appeal involve different, albeit overlapping, issues. (See footnote *, *supra*.)

II.
GROUNDS FOR JURISDICTION.

This is an appeal from the judgment (or decision) of a California Court of Appeal, the Court of Appeal of the State of California, Fourth Appellate District, Division Two. The Court of Appeal denied a timely petition for rehearing pursuant to Rule 27(e) of the California Rules of Court;[2] and on September 16, 1981, the California Supreme Court entered an order, a copy of which is attached hereto at Appendix, p. 35, denying a timely petition for hearing. A notice of appeal from the judgment (or decision) of the Court of Appeal, a copy of which is attached hereto at Appendix, pp. 36-38, was filed October 21, 1981, within ninety days following the denial of a hearing by the California Supreme Court. See *American Railway Express Co. v. Levee*, 263 U.S. 19, 21 (1923).

The statutory provisions that give this Court jurisdiction over the within appeal are 28 U.S.C. §1257(1) and 28 U.S.C. §1257(2).[3]

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[2]Rule 27(e) of the California Rules of Court provides in pertinent part as follows:

> "If no order is made before the decision becomes final as provided in subdivision (a) of rule 24, the petition shall be deemed denied, and the clerk shall enter a notation in the register to that effect."

[3]Under 28 U.S.C. §1257(1) "[f]inal judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court . . . [b]y appeal, where is drawn in question the validity of a . . . statute of the United States and the decision is against its validity". Here the validity of 12 C.F.R. §545.8-3(f) and (g) was drawn into question and the decision is effectively against its validity. See *Wissner v. Wissner*, 338 U.S. 655 (1950). Accordingly, 28 U.S.C. §2403(a) may be applicable herein.

Under 28 U.S.C. §1257(2) "[f]inal judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court . . . [b]y appeal where is drawn in question the validity of a statute of any state on the ground of it being repugnant to the Constitution . . . or laws of the United States, and the decision is in favor of its validity". Here the validity of California Civil Code §711 was drawn into question on the ground of its being repugnant to the Constitution, HOLA, and 12 C.F.R. §545.8-3(f) and (g) insofar as it purports to apply to the "due-on-sale" practices of federally chartered savings and loan associations, and the decision is in favor of its validity. See *McCarty v. McCarty*, ___U.S. ___, 101 S.Ct. 2728, 2734 n. 12 (1981). Accordingly, 28 U.S.C. §2403(b) may be applicable herein.

III.
GERMANE CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS.

The constitutional provisions, statutes and regulations germane to the within appeal are as follows:

1. Article VI, Clause 2 of the United States Constitution ("the Supremacy Clause").

2. Article I, Section 8, Clause 3 of the United States Constitution ("the Commerce Clause").

3. Section 5(a) of the Home Owners' Loan Act of 1933, 12 U.S.C. §1464(a), which provides, in pertinent part, as follows:

> "[T]he [Federal Home Loan Bank] Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations'. . . ."

4. A regulation promulgated by The Federal Home Loan Bank Board, 12 C.F.R. §545.8-3(f) and (g), which provides, in pertinent part, as follows:

> "*Due-on-sale clauses*. An association continues to have the power to include, as a matter of contract between it and the borrower, a provision in its loan instrument whereby the association may, at its option, declare immediately due and payable sums secured by the association's security instrument if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent.
>
> * * *
>
> "[E]xercise by the association of such option (hereafter called a due-on-sale clause) shall be exclusively governed by the terms of the loan contract, and all rights

and remedies of the association and borrower shall be fixed and governed by that contract."

5. 12 C.F.R. §556.9(j); see 46 Fed. Reg. 39,123, 39,124 (1981).

6. California Civil Code §711:

"Conditions restraining alienation, when repugnant to the interest created, are void."[4]

IV.
STATEMENT OF THE CASE.

In 1977, Appellant Glendale Federal Savings and Loan Association ("Glendale Federal") made a loan to William K. Horsman ("Horsman") to finance Horsman's purchase of real property commonly known as 13711 Hewes Avenue, Tustin, California ("the subject property"). In connection with that loan Glendale Federal and Horsman entered into a mortgage loan contract ("said mortgage loan contract") embodied in (1) a promissory note ("said note") in the principal sum of $66,400.00, bearing interest at 9.25% and repayable in equal monthly installments over thirty years; and (2) a deed of trust ("said deed of trust") from Horsman as trustor in favor of Glendale Federal as beneficiary and Appellant Verdugo Service Corporation ("Verdugo") as trustee, securing payment of said note and authorizing a sale of the subject property under a "power of sale" in the event of a default by Horsman. Approximately one year later, in 1978, Horsman conveyed title to the subject property to Appellees Dean L. Gross and Pedro Enriquez.

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[4]The aforedescribed constitutional provisions, statutes and regulations are set forth, in full, at Appendix, pp. 39-68.

Said mortgage loan contract contains a "due-on-sale" clause (or, more precisely, several "due-on-sale" clauses that, for convenience, shall be referred to in the singular).[5]

Glendale Federal did not consent to the conveyance of the subject property from Horsman to Appellees; and, upon learning that it had occurred, Glendale Federal, pursuant to the aforedescribed "due-on-sale" clause, declared the entire indebtedness evidenced by said note and secured by said deed of trust immediately due and payable. When the indebtedness was not paid, Glendale Federal instituted non-judicial "power of sale" foreclosure proceedings.

On June 18, 1979, Appellees filed in the Orange County Superior Court ("the trial court") a complaint against both Glendale Federal and Verdugo, *Dean L. Gross, et al. v. Glendale Federal Savings & Loan Association, et al.*, O.C.S.C. No. 31-53-45 ("the action below"). The gravamen of the action below was that the "due-on-sale" clause in said mortgage loan contract was invalid and/or could not be enforced upon the transfer of title to the subject property from Horsman to Appellees under various provisions of California law, including Civil Code §711, presumably as interpreted in *Wellenkamp v. Bank of America*, 21 Cal.3d 943, 582 P.2d 970, 148 Cal.Rptr. 379 (1978).

In their answer Glendale Federal and Verdugo alleged, *inter alia*, that Glendale Federal "is a Federal savings and loan association organized and existing under the Home Owners' Loan Act of 1933, . . . and has operated and continues to operate under the continuing supervision and directives of the Federal Home Loan Bank Board"; that "the

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[5]The "due-on-sale" clause in said note provides as follows:

> "The holder shall have the right, at its option, to declare this note, irrespective of the maturity date specified herein, immediately due and payable, or increase the interest rate hereof, if (1) the undersigned sells, enters into a contract of sale, conveys or alienates the property securing this note or any part thereof, or suffers his title to said property or any interest therein to be divested, whether voluntari y or involuntarily. . . ."

validity, force and effect of 'due-on-sale' provisions contained in . . . [mortgage] loan contracts used by Federal savings and loan associations at all times herein relevant have been, and now are, governed exclusively by Federal law and regulation which has preempted, and does now preempt, the application of . . . state laws . . .''; that ''[b]y reason of the foregoing, the 'due-on-sale' provision of the subject deed of trust is exercisable and enforceable . . . according to its express terms . . .''; and, as an affirmative defense, that ''[t]he existence and operation of the Home Owners' Loan Act of 1933, and the regulations promulgated thereunder, as from time to time amended and supplemented, preempt application of the law of California to the claims and matters alleged in said Complaint and, by reason thereof, this action, to the extent it is founded upon the law of California, is barred by each and all of Article I, Section 8, [Clause 3] . . . and by Article VI, Clause 2 of the United States Constitution''.

On September 11, 1979, Glendale Federal and Verdugo filed a notice of motion and motion ''pursuant to [California] Code of Civil Procedure Section 437c, for an order of partial summary judgment in their favor dismissing [Appellees'] Complaint . . . on the grounds, *inter alia*, that federal law has preempted the field of regulation of the use and exercise of 'due-on-sale' clauses by federal savings and loan associations, to the complete exclusion of state law, and that [Appellees'] claims in the Complaint have no basis under federal law'' (''the motion for summary judgment''). In support of the motion Glendale Federal and Verdugo offered as exhibits, *inter alia*, Resolution No. 76-296 of the Bank Board, dated April 28, 1976 (and published at 41 Fed. Reg. 18,286 (1976)), which adopted and promulgated 12 C.F.R. §545.8-3(f) and (g) [(originally 12 C.F.R. §545.6-11(f) and (g))]. The preamble to 12 C.F.R. §545.8-3(f) and (g) provides, *inter alia*, that ''it was and is the [Bank] Board's intent to have . . . due-on-sale practices of Federal asso-

ciations governed exclusively by Federal law . . . [and that] Federal associations shall not be bound by or subject to any conflicting State law which imposes different . . . due-on-sale requirements. . . .'' The text of the regulation itself provides, in pertinent part, that a federal association ''continues to have the power to include, as a matter of contract between it and the borrower'', a ''due-on-sale'' provision; and, subject to certain exceptions not here relevant that ''exercise by the association of . . . [the ''due-on-sale'' clause] shall be governed exclusively by the terms of the loan contract, and all rights and remedies of the association and the borrower shall be fixed and governed by that contract''. (41 Fed. Reg. 18,286, 18,287 (1976).)

On October 18, 1979, the trial court entered an order granting the motion for summary judgment and dismissing with prejudice the complaint of Appellees and, thereafter, it entered a judgment providing, *inter alia*, that:

> ''Federal law, including specifically 12 C.F.R. § 545.6-11(f) and (g) (since renumbered as 12 C.F.R. § 545.8-3(f) and (g)), exclusively governs the validity and exercisability of due-on-sale clauses in the loan instruments of federally-chartered savings and loan associations executed on or after June 8, 1976. California law on the validity and exercisability of due-on-sale clauses does not apply to such loan instruments.'' (See Appendix, pp. 31-32.)

Appellees appealed to the Court of Appeal. The Court of Appeal, in an opinion filed July 23, 1981, rendered its decision reversing the judgment of the trial court. (See Appendix, pp. 1-4.) Subsequently, the Court of Appeal denied a timely Petition for Rehearing (see text accompanying footnote 2, *supra*.) and on September 16, 1981, the California Supreme Court denied a timely Petition for Hearing. (See Appendix, p. 35.)

V.

THE QUESTION IS SUBSTANTIAL.

A. The Question Is Important.

1. Effect Upon the Operation of the Federal Savings and Loan System and the Availability of Mortgage Credit.

Resolution of the question presented will greatly affect the operation of the federal savings and loan system and the availability of mortgage credit to the people of the Nation.

At present there are several thousand federally chartered savings and loan associations, operating in all states of the United States, with aggregate assets of approximately $350 billion dollars. See United States League of Savings Associations, *'81 Savings and Loan Sourcebook*, p. 37 (1981). The determination of the question will profoundly influence, among other things, (1) the future mortgage lending practices of federal savings and loan associations and, in particular, their ability to enter into long-term mortgage loan contracts at fixed rates of interest;[6] (2) the acceptability in the secondary mortgage market of loans made by federal associations;[7] (3) the ability of hundreds of thousands of

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[6]A "due-on-sale" clause is a device in a mortgage loan contract for determining the duration of an extension of credit at a particular interest rate. Yet unlike other devices for fixing the duration of an extension of credit at a particular interest rate, such as an arbitrary due date or a provision for varying the interest rate throughout the life of the loan, it enables the borrower to have the benefit of the extension of credit at the fixed rate for as long as that credit is needed for the purpose for which it is usually obtained—financing the purchase of the real property hypothecated as security for the loan. Without the ability to incorporate into their mortgage loan contracts a "due-on-sale" clause that can be exercised for the purpose of adjusting the interest yield on the extension of credit, federal associations will, as a practical matter, be precluded from offering long-term, fixed rate mortgage loan contracts.

[7]The Federal National Mortgage Association ("FNMA") now requires that all loans to be purchased by it in the secondary mortgage market under the FNMA Resale Finance Program contain either (1) a fully enforceable "due-on-sale" clause, or (2) a "seven-year call option" permitting FNMA to declare the entire outstanding balance of the loan fully due and payable after seven years. See the FNMA letter of December 12, 1980 addressed to "All FNMA Seller/Servicers"; see also *Savings & Loan News*, December 1980, at pp. 6-7.

borrowers from federal savings and loan associations under existing long-term fixed interest rate mortgage loan contracts to exact an unbargained for "windfall" at the expense of both federal association lenders, future borrowers and those in the construction trades by, in effect, "selling" their loans at the time that they sell the real property hypothecated as security for such loans;[8] and (4) the legality of thousands, and perhaps hundreds of thousands, of variable interest rate mortgage loan contracts entered into by federal associations since 1978 that are authorized by federal regulation but would violate state law.[9]

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[8]While the direct impact of such "windfalls" would be upon the federal associations themselves, there would also be a significant indirect impact upon future borrowers who would, at least in part, subsidize this "windfall." See *Occidental Savings & Loan Association v. Venco Partnership*, 206 Neb. 469, 293 N.W.2d 843, 847-849 (1980); *Dunham v. Ware Savings Bank*, ___Mass. ___ , 423 N.E.2d 998, 1003-1004 (1981); *Crestview, Ltd. v. Foremost Insurance Co.*, 621 S.W.2d 816, 824 (Tex.Civ.App. 1981). Moreover, this would be an adverse impact upon the construction trades and owners of unencumbered property caused by a reduction in the availability of funds for new mortgage loans, thereby effectively restraining the alienation of such unencumbered property.

[9]While the opinion of the Court of Appeal purports to address only the question of whether federal law preempts state law pertaining to the "due-on-sale" practices of federal associations, a logical corollary of the decision is that any regulation promulgated by the Bank Board pursuant to HOLA and dealing with the mortgage lending practices of federal associations that is permissive rather than mandatory must yield to state law. Since many, if not most, of the Bank Board regulations dealing with the mortgage lending practices of federal associations are both (1) permissive rather than mandatory, and (2) contrary to certain laws of California, the opinion has serious possible ramifications transcending the "due-on-sale" issue.

For example, under former 12 C.F.R. §545.6-4(a), as amended September 30, 1980, federal associations were (until August 1, 1981) authorized, but not required, to make "renegotiable rate" loans (1) "for a term of up to thirty years"; and (2) without offering the prospective borrower a fixed rate loan in the same amount. See 45 Fed. Reg. 67,059 (1980). Under California Civil Code §1916.8 and §1916.9, however, "renegotiable rate mortgage loans" (1) may not have a term in excess of five years; and (2) in conjunction with the making of each "renegotiable rate" loan the lender must have offered "to a borrower who occupies or intends to occupy the property which is security for the loan . . . a fixed rate mortgage loan in the same amount . . .". (In addition, federal associations, while required to make certain substantially similar disclosures, were not required to make the disclosures to borrowers with respect to "renegotiable rate" loans prescribed by California Civil Code §1916.8.)

(footnote continued on following page)

2. Effect Upon the Ability of the Bank Board to Effectively Regulate the Operation of Federally Chartered Savings and Loan Associations.

Under HOLA the Bank Board has a mandate to regulate the operations of federally chartered savings and loan associations; and in order to discharge that mandate it must have the authority to preempt state laws within the regulated fields. Otherwise the operation of federal associations would be controlled by the vagaries of the laws of fifty different jurisdictions.

The decision of the Court of Appeal, however, vitiates the existence of the requisite preemptive authority. If allowed to stand, it would relegate the Bank Board to the

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Furthermore, under current 12 C.F.R. §545.6-4(a), federal associations are authorized to make variable interest loans known as "adjustable mortgage loans" in which (1) the rate of interest may fluctuate as often as every thirty days; (2) in which the amount of such fluctuation is "uncapped" and (3) in which the rate of interest may change during the first semiannual period. See 46 Fed. Reg. 24,148 (1981). Yet under California Civil Code §1916.5—which explicitly purports to apply to federal associations—(1) the rate of interest on a variable interest rate loan "shall change not more often than once during any semiannual period, and at least six months shall elapse between any two such changes"; (2) "[t]he change in interest rate shall not exceed one-fourth of 1 percent in any semiannual period, and shall not result in a rate more than 2.5 percentage points greater than the rate for the first loan payment due after the closing of the loan"; and (3) "[t]he rate of interest shall not change during the first semiannual period." (Recently the California Legislature enacted a "parity" statute, California Financial Code §7150.1, which will expire by its own terms on December 31, 1983, for the purpose of temporarily overriding the limitations imposed by California Civil Code §1916.5.)

Since the foregoing Bank Board regulations are (1) permissive rather than mandatory and (2) in conflict with state law (at least as it existed prior to the enactment of Financial Code §7150.1), does the opinion of the Court of Appeal mean that all of the loans made by federal associations in California pursuant to such regulations—perhaps aggregating hundreds of millions of dollars—are illegal? Moreover, what about the situation in other states that have restrictions upon adjustable mortgage loans inconsistent with the Bank Board regulations?

function of chartering institutions that, once they came into existence, would be compelled to abide by state laws, however pernicious, inane or incompatible they may be with the policy objectives of HOLA and the Bank Board; and the Bank Board's mandate would be confined to regulating in those interstitial areas not occupied by or, superimposing additional regulations not inconsistent with, state law—an obviously incongruous situation.

In short, while the specific question here presented is whether the mortgage lending practices, and specifically the "due-on-sale" practices, of federally chartered savings and loan associations are subject to state law, the resolution of that question will profoundly affect the ability of the Bank Board to regulate the operations of federally chartered savings and loan associations in other areas as well.[10]

3. Effect Upon the Ability of the Comptroller of the Currency and the National Credit Union Administration to Regulate, Respectively, the Operations of National Banking Associations and Federal Credit Unions.

The within appeal is directly concerned with HOLA and the authority conferred thereby upon a specific federal agency, the Bank Board. Nevertheless, and while there obviously may be critical and dispositive statutory distinctions, resolution of the question here presented will, by analogy, have implications for the ability of the Comptroller of the Currency and the National Credit Union Administration to preempt state laws affecting the operations of national banking associations and federal credit unions.

Whether or not such preemptive authority exists is of immediate—and profound—practical significance.

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[10]The practical consequence of an inability on the part of the Bank Board to preempt state law could, even in the short term and without regard to the "due-on-sale" issue, be extremely grave. See footnote 9, *supra*.

On March 27, 1981, for example, the Comptroller of the Currency promulgated a new regulation, 12 C.F.R. §29.7, authorizing national banking associations to make adjustable-rate mortgages notwithstanding any limitations imposed by state law. (See 46 Fed. Reg. 18,932 (1981)).[11]

More recently, on September 23, 1981, the Comptroller proposed a regulation, 12 C.F.R. §30.1 (see 46 Fed. Reg. 46,964 (1981)), preempting, subject to certain chronological limitations, state laws such as California Civil Code §711 limiting the exercise of "due-on-sale" clauses in all mortgage loan contracts of national banking associations:

> "A national bank may make or purchase a loan, secured by a lien on real property, that includes a clause, known as a due-on-sale clause, giving the lender or any assignee or transferee of the lender the power to declare the entire debt payable if the liened property is transfered to another owner, and *such clause shall be valid and enforceable notwithstanding any law or judicial decision of any state to the contrary*." (46 Fed. Reg. 46,966; emphasis added.)

Similarly, the National Credit Union Administration has authorized federal credit unions both (1) to make adjustable rate mortgage loans regardless of any limitation upon such loans imposed by state law (see 46 Fed. Reg. 38,669 (1981)); and (2) to exercise "due-on-sale" clauses in mort-

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[11]The Comptroller's regulation was also expressly preemptive of state laws limiting the exercise of "due-on-sale" clauses contained in adjustable mortgage loan contracts:

> "National banks offering or purchasing adjustable-rate mortgage loans are not required to allow those loans to be assumed by new purchasers of the mortgaged property, or to allow new purchasers to take title to such property subject to the lien of an adjustable-rate mortgage loan made pursuant to this Part, *regardless of any limitations on the validity or enforceability of due-on-sale clauses found in state law, which limitations are expressly preempted*." (46 Fed. Reg. 18,944; emphasis added.)

gage loan contracts of federal credit unions regardless of state law. (See 46 Fed. Reg. 38,676 (1981).)[12]

Does the decision of the Court of Appeal in the within appeal mean that the Comptroller and the National Credit Union Administration exceeded (or are threatening to exceed) their respective authorities in promulgating or proposing the aforedescribed regulations?

4. Effect Upon the Well Being of the Federal Fisc.

Resolution of the issue will have a substantial impact upon the federal fisc.

Savings accounts in federally chartered savings and loan associations are, of course, insured by a federal agency, the Federal Savings and Loan Insurance Corporation ("the FSLIC") (12 U.S.C. §1726); and, at present, such insurance extends to accounts having an aggregate value of approximately $284 billion. (The source of this figure is unpublished data supplied by the Statistical Division, Office of Policy and Economic Research, Federal Home Loan Bank Board.)

The FSLIC, which also insures most state-chartered savings and loan associations, has assets with a book value of only $6.7 billion and a present market value that is considerably less (Federal Home Loan Bank Board, *Journal*, Sept. 1981, p. 51.) Beyond that, however, it has a statutory right to borrow up to an additional $750,000,000 from the United States Treasury (12 U.S.C. §1725(i)). Moreover, and whatever the statutory borrowing rights of the FSLIC, the United States Government, in order to preserve public confidence in the financial system of the nation, will probably be forced to "stand behind" the FSLIC to the full extent of FSLIC insurance obligations should its resources be exhausted. As one news magazine recently observed:

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[12]While the volume of loans made by national banking associations and federal credit unions in reliance upon these regulations is unknown to Glendale Federal and Verdugo, it is obviously substantial.

"Insured deposits. They're safe. Scare talk says that state and Federal deposit insurance could run dry. But if that ever happened, Congress would have to save you regardless of cost. If people ever lost confidence in deposit insurance, it would start a run on every bank, savings and loan association and credit union in America." (*Is Your Money Safe?*, Newsweek, June 22, 1981, p. 74.)

At the present time the thrift industry in the United States is in severe financial difficulty. During the first six months of 1981 federally-insured savings and loan associations lost approximately $1.5 billion (see Federal Home Loan Bank Board, *News*, press release, Sept. 29, 1981), and projections for the future are extremely gloomy. Indeed, some observers have expressed concern over the very survival of the industry.[13]

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[13] "The earnings pinch our institutions are facing is the most serious in the last three decades," says Richard Pratt, chairman of the Federal Home Loan Bank Board, which regulates the S&L's. 'But we believe that it is a situation within the capability of the industry and our agency to manage.' Still, the thrifts are plainly in a pickle. Attracted by high rates on investments such as Treasury bills and money-market funds, savers have been withdrawing their funds from the institutions in record amounts. In April, for example, the S&L's had a net outflow of $4.6 billion.

"Since 1978 the thrifts have been able to counter some of this 'disintermediation' by issuing their own money-market certificates, pegged to T-bill rates. But the certificates have greatly increased the amount of interest the thrifts must pay to attract savings, while the amount of interest they earn on their long-term, fixed-interest-rate home mortgages has increased more slowly. As a result, the S&L's now have a 'negative spread'—that is, they earn less on their mortgage investments than they pay out on their deposits." (*A Scary Shift From Thrift*, Newsweek, June 22, 1981, p. 70.)

"Last year FSLIC paid out $1.3 billion to acquire the assets of S&Ls it forced to merge. For the five months so far this year the payout has been $577 million. However, the big difference in FSLIC's net cost of S&L mergers and liquidations is the price those assets fetch in the market. In 1980 it sold the $1.3 billion in assets for $1.1 billion. This year it estimates that assets with a book value of $577 million will bring in only $202 million, hence the net $375 million cost to FSLIC.

"This illustrates how much S&L assets have depreciated. Recently economist Alan Greenspan calculated that if thrifts had to liquidate their portfolios, consisting of many low-yielding mortgages, their $31 billion net worth would become a $70 billion deficit." (Washington Post, June 12, 1981 at C.1.)

A factor that seriously exacerbates such financial difficulty is the restrictions that various states have imposed, either by statute or case law, upon the ability of mortgage lenders to exercise "due-on-sale" clauses in their mortgage loan contracts. What such restrictions do, simply stated, is to prolong drastically the life of existing lower-yield mortgage loans and thereby deprive lenders, who must pay essentially the prevailing market rate on lendable funds, of the opportunity to bring the yield on their portfolios into proper ratio with the cost of such lendable funds.[14]

Federally chartered savings and loan associations hold a huge portfolio of low yield mortgage loans secured by real property located in states that restrict exercise of the "due-on-sale" clause. Hence the financial exposure of the federal government attributable to an inability on the part of federal associations to exercise "due-on-sale" clauses in their mortgage loan contracts, although difficult to quantify, is obviously significant. Indeed, in the case of some associations, whether or not they are able to freely exercise the "due-on-sale" clauses in their mortgage loan contracts could well mean the difference between survival and failure; and since any single failure of an insured financial institution can require an expenditure by the FSLIC of hundreds of millions

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[14]For a discussion of the economic impact of restrictions upon the exercisability of "due-on-sale" clauses, see, *e.g.*, Preis & Van Order, "An Economic Analysis of Due-on-Sale Clauses", U.S. Department of Housing and Urban Development, May, 1981; Pratt & Campbell, "An Economic Analysis of the 'Due on Sale' Clause in the California Mortgage Market", Monograph No. 14, Krannert Graduate School of Management, Purdue University Credit Research Center, 1979.

of dollars, the effect upon the federal fisc of even a handful of failures attributable to an inability to exercise the "due-on-sale" clause could be immense.[15]

5. The Importance to Various Federal Agencies of a Prompt Resolution of the Question Presented.

The question presented by the within appeal was recently before the United States Court of Appeals for the Ninth Circuit in appeals by various officials of the State of California, represented by the California Attorney General, from decisions of federal district courts in favor of, *inter alia*, the Bank Board in *Glendale Federal Savings & Loan Association v. Fox*, 459 F.Supp. 903 (C.D. Cal. 1978) and 481 F.Supp. 616 (C.D. Cal. 1979) (9th Cir. No. 79-3573), and *Conference of Federal Savings & Loan Associations v. Stein*, 495 F.Supp. 12 (E.D. Cal. 1979) (9th Cir. No. 79-4818).

It was regarded as of such magnitude that five federal agencies not parties to the *Fox* and *Conference* litigation, including the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Comptroller of the Currency, the Federal Home Loan Mortgage Corporation, and the United States Treasury Department submitted affidavits or declarations in support of a motion by the Bank

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[15] "The estimated cost to the Federal Savings and Loan Insurance Corp. of assisting troubled thrifts in the first five months of this year amounted to $375 million, or 140 percent more than in the comparable period last year. . . . If aid continued at the same level for the rest of the year, it would total $900 million." (Washington Post, June 12, 1981, at C.1.)

The estimated cost to the FSLIC by reason of the recent liquidation of a single relatively small institution, Economy Savings and Loan Association of Chicago, was $60.2 million. *Id.*

Board that the within appeals be decided on an expedited basis.[16]

B. There Is a Divergence of Authority With Respect to the Question Presented.

There is a divergence of authority in the Nation, and even within the judicial system of the State of California itself, with respect to the question presented.

On the one hand, a host of courts, including every federal court that has decided the question, many state courts and even an intermediate appellate court in California, have concluded that federal law *does* preempt state law with respect to the "due-on-sale" practices of federal associations. See, *e.g.*, *Price v. Florida Federal Savings & Loan Association*, No. 79-974 (M.D. Fla., Sept. 1, 1981); *First Federal Savings & Loan Association of Gadsden County v. Peterson*, 516 F.Supp. 732 (N.D. Fla. 1981); *Collins v. First Federal Savings & Loan Association of Walla Walla*, No. C-80-334 (E.D. Wash., May 18, 1981); *First Federal Savings & Loan Association of Phoenix v. Development & Management Enterprises, Inc.*, No. CIV 79-880 PHX-EHC (D. Ariz., April 2, 1981); *Dantus v. First Federal Savings & Loan Association of Denver*, 502 F.Supp. 658 (D. Colo. 1980); *Great Western Union Federal Savings & Loan Association v. Walters*, No. C 79-906V (W.D. Wash., June 18, 1980); *Williams v. First Federal Savings*

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[16]The affidavits and declarations were executed, respectively, by the Chairman of the Federal Deposit Insurance Corporation, William M. Issac; the Chairman of the National Credit Union Administration, Lawrence Connell; the Senior Deputy Comptroller for Bank Supervision for the Office of the Comptroller of the Currency, Paul M. Homan; the President of the Federal Home Mortgage Loan Corporation, Philip R. Brinkerhoff; and the Acting Secretary of the United States Treasury Department, R. J. McNamar.

While the United States Court of Appeals did rule, it decided the cases on procedural grounds without reaching the preemption issue. A petition asking this Court to review the decision of the Court of Appeals will be filed shortly.

& Loan Association of Arlington, 500 F.Supp. 307 (E.D. Va. 1980), *aff'd on other grounds*, 651 F.2d 910 (4th Cir. 1981); *Conference of Federal Savings & Loan Associations v. Stein*, 495 F.Supp. 12 (E.D. Cal. 1979), *rev'd on other grounds*, No. 79-4818 (9th Cir., Sept. 23, 1981); *Bailey v. First Federal Savings & Loan Association of Ottawa*, 467 F.Supp. 1139 (C.D. Ill. 1979); *Glendale Federal Savings & Loan Association v. Fox*, 459 F.Supp. 903 (C.D. Cal. 1978) and 481 F.Supp. 616 (C.D. Cal. 1979), *rev'd on other grounds*, No. 79-3573 (9th Cir., Sept. 23, 1981); *People v. Glendale Federal Savings & Loan Association*, 122 Cal.App.3d 860, 176 Cal.Rptr. 353 (1981); *Haugen v. Western Federal Savings & Loan Association of Denver*, No. 80 CA 0551 (Col.App., April 30, 1981); *Northwestern Federal Savings & Loan Association v. Ternes*, No. 12,694 (Dist. Ct., So. Cen. Jud. of N.D., March 12, 1981); *Fischer v. First Federal Savings & Loan Association of Lenawee County*, No. 80-01-756 (Circuit Ct., Lenawee Co., Mich., Jan. 19, 1981).[17]

On the other hand, the Minnesota Supreme Court, in expansive *obiter dicta* in *Holiday Acres No. 3. v. Midwest Federal Savings & Loan Association of Minneapolis*, ___ Minn. ___, 308 N.W.2d 471 (1981), has stated its view that federal law *does not* preempt state law with respect to "due-on-sale" clauses contained in the mortgage loan instruments of federal savings and loan associations; and two

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[17]On October 28, 1981, the California Supreme Court, while denying a petition for hearing in *People v. Glendale Federal Savings & Loan Association, supra*, directed the California Reporter of Decisions, pursuant to Article VI, Section 14 of the California Constitution and Rule 976 of the California Rules of Court, "not to publish . . . the opinion . . . in the Official Reports . . ." Under Rule 977 of the California Rules of Court "[a]n opinion of a Court of Appeal . . . that is not published in the Official Reports shall not be cited by a court or by a party in any other action or proceeding . . ." that is, presumably, subject to the California Rules of Court. Hence the effect of the California Supreme Court's order of decertification is to eliminate the precedential value of the decision in the California court system.

other California courts, including the Court of Appeal in the within appeal, seizing upon the *dicta* in *Midwest Federal*, have concurred. See *Panko v. Pan American Federal Savings & Loan Association*, 119 Cal.App.3d 916, 174 Cal.Rptr. 240, *appeal docketed*, No. 81-922 (U.S. 1981); *de la Cuesta v. Fidelity Federal Savings & Loan Association, supra*.

Thus, while the weight of authority clearly favors the view that federal law *does* preempt, there is a divergence of authority upon the point—a divergence that only this Court can resolve.

C. The Decision of the Court of Appeal in the Within Appeal Should Be Summarily Reversed.

1. Existing Case Law Overwhelmingly Supports the Conclusion That Federal Law Exclusively Governs the Validity and Exercisability of "Due-On-Sale" Clauses Included in the Loan Instruments of Federal Savings and Loan Associations.

The applicable legal authorities overwhelmingly support the conclusion that federal law, specifically HOLA and the regulatory scheme promulgated thereunder by the Bank Board, has preempted state law with respect to the mortgage lending practices of federally chartered savings and loan associations in general, and the "due-on-sale" practices of such associations in particular.

In its recent decision in *Conference of Federal Savings & Loan Associations v. Stein*, 604 F.2d 1256 (9th Cir. 1979), *aff'd mem.*, 445 U.S. 921 (1980), which held that the procedural aspects of California's "fair lending" laws were inapplicable to federal associations, the Ninth Circuit observed as follows:

> "The Home Owners' Loan Act of 1933, 12 U.S.C. §§1461 et seq. (HOLA), was the result of congressional dissatisfaction with state law and practice in the financing of home construction. The first federal effort

was through the Home Loan Bank Act of 1932. This failed to attack the problem satisfactorily.

* * *

"The result was HOLA, a radical and comprehensive response to the inadequacies of the existing state systems. A *federal* savings and loan system was created. The Federal Home Loan Bank Board (the Bank Board) was created with extremely broad powers to promulgate rules and regulations.

* * *

"With reference to HOLA, one writer has stated: '. . . the states had developed a hodgepodge of savings and loan laws and regulations, and Congress hoped that FHLBB [Bank Board] rules would set an example for uniform and sound savings and loan regulations.' "

* * *

"In our judgment the regulatory control of the Bank Board over federal savings and loan associations is so pervasive as to leave no room for state regulatory control. As this court noted in *Meyers v. Beverly Hills Federal Savings & Loan Ass'n*, 499 F.2d 1145, 1147 (9th Cir. 1974):

'Pursuant to its valid statutory authority, the Federal Home Loan Bank Board has promulgated comprehensive regulations covering all aspects of every federal savings and loan association "from its cradle to its corporate grave." ' " (604 F.2d 1257-1258, 1260; citations omitted.)[18]

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[18]The Ninth Circuit in *Conference* did not decide the question of whether federal law preempted the substantive, as contrasted with the procedural, aspects of California's "fair lending" laws. *In addressing the matter, however, it expressly recognized that if federal law did not preempt the substantive aspects of California's "fair lending" laws, it was because other federal statutes (i.e., federal antidiscrimination laws) overrode the preemption that would otherwise have been effected by HOLA and regulations of the Bank Board promulgated thereunder —not because HOLA and the regulations promulgated thereunder would themselves have failed to preempt.* (See 604 F.2d 1260.)

In *Meyers v. Beverly Hills Federal Savings & Loan Association*, 499 F.2d 1145 (9th Cir. 1974), an action against, *inter alia*, eight federal associations, the plaintiffs challenged the legality of provisions of the mortgage loan contracts of the defendants authorizing them to assess charges in the event that the principal of a loan was repaid prior to maturity, contending that such provisions were void as illegal under former California Civil Code §§1670 and 1671. The federal District Court dismissed the action as against the federally chartered associations on the ground that federal law had preempted the field, rendering §§1670 and 1671 inapplicable to the mortgage loan contracts of such associations. (499 F.2d 1146.) On appeal the Ninth Circuit, after reviewing the doctrine of federal preemption, held that federal law had preempted the regulation of federal associations by reason of the Bank Board's promulgation of comprehensive regulations covering all aspects of their operations, explaining:

> ". . . All of the appellee federal savings and loan associations operate and are organized and chartered under the Home Owners' Loan Act of 1933, 12 U.S.C. Section 1461 et seq. This Act established the Federal Home Loan Bank Board, which 'is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as "Federal Savings and Loan Associations", and to issue charters therefor. . . .' 12 U.S.C. §1464(a).
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> "Pursuant to its valid statutory authority, the Federal Home Loan Bank Board has promulgated comprehensive regulations covering all aspects of every federal

savings and loan association 'from its cradle to its corporate grave.' " (499 F.2d 1146-1147.)[19]

Similarly, in *First Federal Savings & Loan Association of Boston v. Greenwald*, 591 F.2d 417 (1st Cir. 1979), the United States Court of Appeals for the First Circuit was confronted with the question of whether a state law requiring the payment of interest on funds held by federal associations in escrow to defray taxes and insurance on real property hypothecated as security for loans was preempted by HOLA and a regulation of the Bank Board promulgated thereunder, 12 C.F.R. §545.6-11(c). The Court answered that question in the affirmative, explaining:

"The Supremacy Clause . . . requires the invalidation of any state law that either falls within an area exclusively occupied by federal law or actually conflicts irreconcilably with a federal law. We think that Mass.G.L. c. 183, § 61, as applied to federal savings and loan associations, actually conflicts with 12 C.F.R. § 545.6-11(c) and therefore is preempted . . .

"The Home Owners' Loan Act grants to the Bank Board broad regulatory authority over the operation of federal savings and loan associations [citation omitted]. Pursuant to this authority, the Bank Board has issued detailed regulations governing the 'operations of every Federal savings and loan association from its cradle to

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[19]With respect to the specific area of controversy in *Meyers*, prepayment charge provisions in mortgage loan contracts, the Ninth Circuit answered the contention that such contractual provisions in the mortgage loan contracts of federal associations were invalid under former Cal. Civ. Code §§1670 and 1671 as follows:

"Section 545.6-12(b) [specifically covering the area of prepayment charges] represents a valid exercise of the Federal Home Loan Bank Board's delegated power, and we therefore hold *that federal law preempts the field of prepayments of real estate loans to federally chartered savings and loan associations, so that any California law in the area is inapplicable to federal savings and loan associations operating within California.*" (499 F.2d 1147; emphasis added; footnotes omitted.)

its corporate grave'. One such regulation is 12 C.F.R. § 545.6-11(c), which specifies the conditions under which the federal associations must pay interest on escrow accounts . . . ." (591 F.2d 425.)

See also, *e.g.*:

First Federal Savings and Loan Association of Boston v. State Tax Commission, 437 U.S. 255, 258 n. 3 (1978) [". . . the federal statute [HOLA] protects federal associations from being forced into the state regulatory mold . . . ."];

People v. Coast Federal Savings and Loan Association, 98 F.Supp. 311, 316 (S.D. Cal. 1951).

With respect to the particular mortgage lending practice here in question, there is a plethora of cases holding that federal law preempts state law with respect to the validity and exercisability of "due-on-sale" clauses contained in the mortgage loan contracts of federal associations. (See §V.B., *supra*.)

2. The Opinion of the Court of Appeal Is Replete With Legal Errors, Misstatements and Omissions.

(a) *The Opinion Draws a Distinction Between the "Internal" and "External" Affairs of Federal Associations That Is Not Supported, and Indeed Is Plainly Confuted, by the Pertinent Case Law.*

The opinion characterizes a series of reported cases that have found preemption, including *Conference of Federal Savings & Loan Associations v. Stein*, 604 F.2d 1256 (9th Cir. 1979), *aff'd mem.*, 445 U.S. 921 (1980); *Meyers v. Beverly Hills Federal Savings & Loan Association, supra*; *Kaski v. First Federal Savings & Loan Association of Madison*, 72 Wis.2d 132, 240 N.W.2d 367 (1976); *Derenco, Inc. v. Benj. Franklin Federal Savings & Loan Association*, 281 Or. 533, 577 P.2d 477 (1978), *cert. denied*, 439 U.S. 1051 (1978); and *Sears v. First Federal Savings & Loan Association of Chicago*, 1 Ill App.3d 621, 275 N.E.2d 300

(1971) as dealing with the "internal" affairs of federal savings and loan associations, in contradistinction to the case at bar which, presumably, deals with the "external" affairs of such associations. (121 Cal.App.3d 340-341, 175 Cal.Rptr. 474.)[20]

The contradistinction is patently invalid. Each of the afore-cited cases deals with *an aspect of the mortgage lending practices of federal associations*, just as the within action deals with *an aspect of the mortgage lending practices of federal associations*.[21] Upon what conceivable basis, therefore, can a distinction legitimately be drawn in the within action based upon the "internal vs. external" affairs criterion?[22]

(b) *The Opinion Resolves the Preemption Issue Based Upon an Incorrect and Illogical Analysis.*

The opinion acknowledges that "the *Board* has manifested *its* unqualified intention that the adopted regulations and implementing policy relating to due-on-sale clauses

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[20]References herein to "the opinion" of the Court of Appeal are, necessarily, to the opinion in *de la Cuesta v. Fidelity Federal Savings & Loan Association, supra*. (See footnotes * and 1, *supra*.)

[21]*Conference of Federal Savings & Loan Associations v. Stein, supra*, dealt with the "fair lending" practices of federal associations; *Meyers v. Beverly Hills Federal Savings & Loan Association, supra*, dealt with the prepayment charge practices of federal associations; *Kaski v. First Federal Savings & Loan Association of Madison, supra*, dealt with the interest escalation practices of federal associations; *Derenco, Inc. v. Benj. Franklin Federal Savings & Loan Association, supra*, dealt with the payment of interest on escrow account practices of federal associations; and *Sears v. First Federal Savings & Loan Association of Chicago, supra*, dealt with the practices of federal associations with respect to the payment of interest upon funds held by federal associations to defray real estate taxes and insurance on real property hypothecated as security for loans.

[22]Moreover, the opinion does not even attempt to distinguish other prominent decisions holding that federal law preempts state law with respect to the mortgage lending practices of federal associations. See, *e.g., First Federal Savings & Loan Association of Boston v. Greenwald*, 591 F.2d 417, 425 (1st Cir. 1979). Furthermore, the opinion simply ignores, without any citation, analysis or distinction, a vast body of case law holding that federal law *does* preempt the "due-on-sale" practices of federal associations. (See §V.B., *supra*.)

shall occupy a preemptive position over conflicting state law provisions''; yet it concludes that there is no preemption not because the regulation is invalid but, rather, because it does not necessarily conflict with state law. (121 Cal.App.3d 339, 175 Cal.Rptr. 473; emphasis in original.)

This analysis is both incorrect and illogical. First of all, there *is* a necessary conflict. (See §V.C.2.(c), *infra*.) Furthermore, if the regulation is *valid* and *intended to preempt*, *ipso facto* it *does* preempt; and if it is *not* valid, then whether or not there is a ''necessary conflict'' between the regulation and state law is irrelevant—there is simply no valid federal regulation.

In short, since the preemptive intent of the federal ''due-on-sale'' regulation is clear, it could fail to preempt only if it was invalid; and given the plenary delegation of authority over the operation of federally chartered associations contained in HOLA and the overwhelming body of case law interpreting it, the regulation clearly is *not* invalid.

(c) *The Opinion Ignores a Fundamental Conflict Between the Federal ''Due-On-Sale'' Regulation and State Law.*

The opinion states that since ''[t]he federal [due-on-sale] regulation merely authorizes and does not compel savings and loan associations to include a due-on-sale clause in their loan contracts and to exercise their rights thereunder . . . the federal loan association is not faced with physical impossibility in complying with the two regulatory schemes''; and, accordingly, that ''[t]here is no 'inevitable collision' between the two regulations''. (121 Cal.App.3d 341, 175 Cal.Rptr. 475.) This reasoning is faulty.

While it may be true that the federal ''due-on-sale'' regulation does not mandate the inclusion or exercise of ''due-on-sale'' clauses and that therefore a federal association could theoretically comply with both, it *does* mandate that federal associations shall have the *option* to include and

exercise such clauses *without regard to any limitations imposed by state law. In other words, the regulation authorizes federal associations to do something that state law may prohibit them from doing. How much clearer a conflict or inconsistency could there be*? See, *e.g., Sanders v. Federal National Mortgage Association*, 393 F.Supp. 739, 740 (E.D. La. 1975).[23]

(d) *The Opinion Is Wrong in Concluding That There Was No Congressional Intent to Permit Preemption as to the "Due-on-Sale" Practices of Federal Associations.*

The opinion concludes that Congress did not intend to permit preemption as to the "due-on-sale" clauses of federal associations. (121 Cal.App.3d 339, 175 Cal.Rptr. 473-474.) The conclusion is erroneous.

The language used by Congress in §5(a) of HOLA, *i.e.*, that "the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation and regulation" of federal associations, itself clearly indicates that Congress intended to authorize the Bank Board to preempt state law regarding the mortgage lending practices of federal associations. In addition to the language of HOLA itself, the legislative history indicates that Congress intended that the Bank Board would have the authority to preempt state law with respect to the mortgage lending practices of federal associations. Finally, any remaining doubt regarding the intent of Congress has been resolved by congressional af-

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[23]Moreover, an "inevitable collision" is not a prerequisite to the existence of preemption. In *Meyers v. Beverly Hills Federal Savings & Loan Association, supra*, for example, a federal regulation which authorized—but did not require—the imposition of a prepayment charge in the event that a loan was paid off prior to its specified maturity was held to preempt state law limiting such charges.

firmation of administrative and judicial interpretations of HOLA. (See §V.C.2.(e), *infra*.)[24]

(e) *The Opinion Ignores the Principle That When Congress Amends a Statute Without Overruling Prior Judicial or Administrative Interpretations, It Is Presumed That the Prior Interpretations Were in Accord With the Intent of Congress.*

When (1) a statute is interpreted in a particular manner by a court or the governmental agency responsible for administering the statute, and (2) Congress, although it has an opportunity to do so (as, for example, when Congress amends another part of the statute) does not amend the statute to alter the judicial or administrative interpretation thereof, the interpretation reached by the court or agency is presumed correct. As this Court stated in *Lorillard v. Pons*, 434 U.S. 575, 580-581 (1978):

> "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it reenacts a statute without change." (Citations omitted.)

See also, *e.g.*, *Francis v. Southern Pacific Co.*, 333 U.S. 445, 450 (1948); *Rath Packing Co. v. Becker*, 530 F.2d 1295, 1312 (9th Cir. 1975), *aff'd sub nom., Jones v. Rath Packing Co.*, 430 U.S. 519 (1977); *Bennett v. Panama Canal Co.*, 475 F.2d 1280, 1282 (D.C. Cir. 1973).

Courts throughout the nation have previously interpreted HOLA as intended to preempt state law regarding the mortgage lending practices of federal associations. With respect

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[24]Moreover, the opinion misdescribes a provision of HOLA. It states that "[t]he Home Owners' Loan Act specifically provides that federal savings and loan associations are . . . not exempt from more stringent state laws on neighborhood discrimination or consumer credit protection", citing 12 U.S.C. §1464(a)(i). (121 Cal.App.3d 335, n. 5, 175 Cal.Rptr. 471.) In fact, the provision in 12 U.S.C. §1464(a)(i) alluded to concerns *state-chartered savings banks* that convert to federal charters, *not* federally chartered savings and loan associations generally.

to the Bank Board's interpretation of its own powers, 12 C.F.R. §545.8-3(f) and (g), which, as the Court of Appeal has acknowledged, was clearly and explicitly intended to preempt state law, was widely disseminated in 1976. Since that time, and in spite of numerous opportunities to do so, and in spite of congressional awareness and discussion of the matter, Congress, in enacting amendments to §5(a) of HOLA on at least six different occasions, has not acted to reject or alter the interpretation of HOLA reached by the courts and by the Bank Board. This lack of reaction on the part of Congress conclusively establishes that Congress did and does intend that HOLA and the regulations of the Bank Board should preempt any contrary state law regarding the mortgage lending practices of federal associations.[25]

In summary, the conclusion that federal law has preempted state law with respect to the "due-on-sale" practices of federal associations is ineluctable.

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[25]In reaching its conclusion, the opinion has mischaracterized the relevance herein of considerations of federalism. It states that "[t]he decision whether to displace state law is a fundamental one going to the very fabric of federalism; thus, the decision is one to be made by the people through their elected representatives in Congress rather than by agencies or tribunals insulated from democratic pressures." (121 Cal.App.3d 339-340, 175 Cal.Rptr. 474); citing *City of Milwaukee v. Illinois*, ___U.S. ___, 101 S.Ct. 1784 (1981).

Actually what *City of Milwaukee, supra,* said was merely that the decision to displace state law should be made by Congress rather than the federal judiciary. (See 101 S.Ct. 1790.) Moreover, the decision in *City of Milwaukee* concerned whether a federal statute had preempted the application of federal common law; the preemption of state law was not an issue therein. Compare *Illinois v. City of Milwaukee*, 406 U.S. 91, 102 (1972).

Congress *does* have the power to delegate to a federal agency the power to preempt state law. See, *e.g., City of Boston v. Harris*, 619 F.2d 87 (1st Cir. 1980). Furthermore, HOLA and the regulations of the Bank Board promulgated thereunder do not displace state law from existing institutions; rather, they provide that state law shall not extend to a creation of the federal government—the federal savings and loan system.

VI.
CONCLUSION.

This Court should either (1) summarily reverse the decision of the Court of Appeal or (2) note probable jurisdiction.

Dated: December 14, 1981.

Respectfully submitted,

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Appendix

APPENDIX.

California Court of Appeal Decision in the Within Appeal.

[Civ. No. 21903. Fourth Dist., Div. Two July 23, 1981.]

Dean L. Gross, et al., Plaintiffs and Appellants, v. Glendale Federal Savings and Loan Association, et al., Defendants and Respondents.

OPINION

APPEAL from a judgment of the Superior Court of Orange County. Edward J. Wallin, Judge. Reversed.

COUNSEL

John W. Dumas for Plaintiffs and Appellants.

McKenna & Fitting, Aaron M. Peck, Terry A. Fralich and C. Steven McMurry for Defendants and Respondents.

This is an appeal from summary judgment in favor of defendant Glendale Federal Savings and Loan Association (hereinafter Glendale Federal). The dispositive issue is whether federal preemption precludes application to a federally chartered savings and loan association of the rule in *Wellenkamp v. Bank of America* (1978) 21 Cal.3d 943, that an institutional lender may not exercise a due-on-sale clause in a deed of trust encumbering residential real property unless the sale or transfer of the property has impaired or threatens to impair the security. The disposition of the appeal is governed by our opinion in the case of *Reginald D. de la Cuesta, et al. v. Fidelity Federal Savings & Loan Association, et al.*, 4 Civil 23253, certified for publication and filed July 2, 1981.

FACTS

This action was commenced by plaintiffs Dean L. Gross and Pedro Enriquez seeking, primarily, declaratory and injunctive relief against the thr :atened foreclosure by trustee's

sale of a deed of trust encumbering residential real property purchased by them, following the purported exercise of a due-on-sale provision in the deed of trust by Glendale Federal, the beneficiary named in the deed of trust.

Glendale Federal moved for summary judgment on the ground that federal preemption precludes application of the *Wellenkamp* rule to a federally chartered savings and loan association. The trial court granted summary judgment and plaintiffs appeal.

Glendale Federal is a private mutual savings and loan association chartered by the Federal Home Loan Bank Board pursuant to Section 5(a) of the Federal Home Owners' Loan Act of 1933 (12 U.S.C. §§1461-1470). On July 15, 1977, Glendale Federal made a loan of $66,400 to William K. Horsman secured by a deed of trust on his residential real property located at 13711 Hewes Avenue, Santa Ana, in the State of California. The deed of trust contained a due-on-sale clause purportedly giving Glendale Federal the right to declare the unpaid balance of the loan immediately due and payable in the event the property or any interest therein was sold or otherwise transferred or conveyed by the borrowers.

On October 24, 1978, Horsman sold and conveyed the property to plaintiffs.

Having learned of the October 24 transfer of the property, Glendale Federal gave notice that it was exercising the due-on-sale clause in the deed of trust, and on March 2, 1979, caused to be recorded a notice of default and election to sell under the deed of trust. Whereupon this action was instituted.

DISCUSSION AND DISPOSITION

Preliminarily, Glendale Federal contends that the issue of federal preemption of state law with respect to enforcement of a due-on-sale clause by a federal savings and loan

association is res judicata between the parties as a result of the federal court decisions of *Conference of Federal Sav. & Loan Ass'ns v. Stein* (9th Cir. 1979) 604 F.2d 1256, *Glendale Fed. Sav. & Loan Ass'n v. Fox* (C.D. Cal. 1978) 459 F.Supp. 903, and *Glendale Federal Sav. and Loan Ass'n v. Fox* (C.D. Cal. 1979) 481 F.Supp. 616. The contention is not meritorious.

It is of course true that members of the public have on occasion been held bound by an earlier adjudication adverse to a public agency on public questions or questions as to which the public agency was authorized to represent the public. (E.g., *Price v. Sixth District Agricultural Assn.* (1927) 201 Cal. 502 [authority of public agency to enter into contract]; *Rynsburger v. Dairymen's Fertilizer Coop., Inc.* (1968) 266 Cal.App.2d 269 [existence of a public nuisance].) However, the rule alluded to has no application to the case at bench. While the question presented is of public interest, it is not a public question. The question is whether a federal savings and loan association may exercise the due-on-sale clause in a deed of trust on account of sale of the encumbered property without any showing that that is reasonably necessary to prevent impairment of its security or to protect against risk of default. The question is one of private property and contract rights, arising between a party to the loan transaction and the other party's successor in interest. It is true that in the federal decisions cited, the courts purported to decide whether the application of state law in respect to due-on-sale clauses in trust deeds of federal savings and loan associations had been federally preempted, but courts do not decide abstract legal questions. None of those cases involved an attempt by a federal savings and loan association to exercise its due-on-sale clause in the absence of reasonable necessity for so doing, which is the question presented here, and in none of the cited cases did

the question arise as between the savings and loan association and the debtor or the debtor's successor in interest to the encumbered property. Neither the parties nor the issue is the same, and the question is not res judicata.

The remaining issues on appeal are comprehensively treated and disposed of in our opinion in *Reginald D. De La Cuesta, et al. v. Fidelity Federal Savings & Loan Association*, 4 Civil 23253, filed July 2, 1981. For the reasons stated and upon the authorities cited therein, we conclude that application of the state law as set forth in *Wellenkamp v. Bank of America, supra*, 21 Cal.3d 943, is not precluded by federal preemption and that the *Wellenkamp* rule is applicable in this case.

Accordingly, the judgment is reversed for further proceedings consistent with this opinion and the opinion in 4 Civil 23253.

Kaufman
Acting P.J.

We concur:
McDaniel, J.
Hyde, J.*

[Not to be Published in Official Reports]

*Appointed by the Chairperson of the Judicial Council.

California Court of Appeal Decision in de la Cuesta v. Fidelity Federal Savings & Loan Association

[Civ. No. 23253. Fourth Dist., Div. Two July 2, 1981.]

REGINALD D. de la CUESTA et al., Plaintiffs and Appellants, v. FIDELITY FEDERAL SAVINGS AND LOAN ASSOCIATION, Defendant and Respondent. ALPHONSO MOORE et al., Plaintiffs and Appellants, v. FIDELITY FEDERAL SAVINGS AND LOAN ASSOCIATION, Defendant and Respondent. JOHN D. WHITCOMBE, Plaintiff and Appellant, v. FIDELITY FEDERAL SAVINGS AND LOAN ASSOCIATION, Defendant and Respondent.

SUMMARY

In each of three consolidated cases against a federally chartered savings and loan association, the purchaser of real property encumbered by a deed of trust sought declaratory and injunctive relief against threatened foreclosure by trustee's sale following defendant's purported exercise of the trust deed's due-on-sale clause. Plaintiffs moved for summary judgment, asserting that state law precluded defendant association from exercising the due-on-sale clauses absent a showing of an impairment to its security or risk of default as a result of the outright sale of the properties to plaintiffs. While conceding that it could not make such a showing, thus rendering the due-on-sale clauses unenforceable under state law, defendant made cross-motions for summary judgment on the ground that the application of state law was precluded by federal preemption. The trial court granted defendant's motion in each case. (Superior Court of Orange County, Nos. 286474, 306349, 308527, Edward J. Wallin, Judge.)

The Court of Appeal reversed. The court held that the state law limitation on the enforcement of due-on-sale

clauses in deeds of trust to instances when the lender can demonstrate that enforcement is reasonably necessary to protect against impairment to its security or the risk of default is not preempted by federal regulations authorizing federal savings and loan associations to include a due-on-sale clause in their loan contracts and to exercise their rights thereunder and requiring that loan instruments provide for full protection to the lender, or on the basis of the "occupation of the field" doctrine, and is thus applicable to federal savings and loan associations. In so holding, the court noted that the Home Owners' Loan Act (12 U.S.C. §§1461-1470; creating the Federal Home Loan Bank Board and authorizing establishment of federal savings and loan associations) is silent with respect to due-on-sale clauses or other loan details and that state law pertaining to the exercise of due-on-sale clauses does not infringe upon and is not otherwise incompatible with the regulation or control of federal savings and loan associations. The court also held that the state law at issue is applicable to commercial as well as residential real property. (Opinion by Kaufman, Acting P. J., with McDaniel and Morris, JJ., concurring.)

COUNSEL

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George Deukmejian, Attorney General, Joseph M. O'Heron, Deputy Attorney General, Richard M. Mosk, W. Gary Kurtz, John R. Hetland, Charles A. Hansen and John W. Dumas as Amici Curiae on behalf of Plaintiffs and Appellants.

Hahn, Cazier & Leff, Andrew E. Katz, Steven G. Polard and Walter L. Blackwell III for Defendant and Respondent.

Henry L. Judy, Maud Mater, Gary S. Smuckler, Marilyn E. Nathanson and Mark C. Ellenberg as Amici Curiae on behalf of Defendant and Respondent.

OPINION

KAUFMAN, Acting P. J.

INTRODUCTION

This is an appeal from summary judgment in favor of defendants in three cases consolidated in the trial court. Where appropriate, the cases will be referred to as the *de la Cuesta* case, the *Moore* case, and the *Whitcombe* case. Each action was commenced by the purchaser of property encumbered by a deed of trust seeking declaratory and injunctive relief against threatened foreclosure of the deed of trust by trustee's sale following the purported exercise of the trust deed's due-on-sale clause. The principal defendant in each action is the beneficiary named in the deed of trust, Fidelity Federal Savings and Loan Association, and the defendants will be referred to collectively as Fidelity Federal. The plaintiffs made motions for summary judgment asserting that in the absence of any showing it was reasonably necessary to avoid impairment of the security or risk of default resulting from the sale, Fidelity Federal was precluded from exercising the due-on-sale clause by the California law as set forth in *Wellenkamp v. Bank of America* (1978) 21 Cal.3d 943 [148 Cal.Rptr. 379, 582 P.2d 970]. The trial court granted Fidelity Federal's cross-motion for summary judgment on the ground that application of the state law is precluded by federal preemption.

The principal issues are whether the trial court correctly determined that application of the state law has been federally preempted and, in the Moore and Whitcombe cases, the effect of a provision in each deed of trust that it "shall be governed by the law of the jurisdiction in which the

Property is located." A determination that there has been no federal preemption of the state law raises an additional issue in the de la Cuesta case as to whether or not the rule announced in *Wellenkamp* applies to commercial, income-producing property. We have concluded that application of the state law has not been federally preempted and that the *Wellenkamp* rule does preclude exercise of the due-on-sale clause in the deed of trust encumbering the commercial property involved in the de la Cuesta case. Accordingly, we reverse the judgment as to each case with directions to the trial court to enter summary judgment in favor of the plaintiffs.

On June 1, 1981, after oral argument and after unanimous agreement of the panel members as to the proper disposition of the issues and the appeal, but before the opinion could be prepared, Division One of the First Appellate District of the Court of Appeal filed its opinion in the case of *Panko v. Pan American Fed. Sav. & Loan Assn.* (1981) 119 Cal.App.3d 916 [174 Cal.Rptr. 240]. In that case in respect to the federal preemption issue the court reached conclusions identical to those reached by us, based on reasoning with which we agree. The reasons and conclusions were ably and succinctly stated in the *Panko* opinion, and it would serve no useful purpose for us to attempt to craft a wholly original opinion. On the other hand, inasmuch as the *Panko* decision is not yet final, it is inappropriate that we simply cite it as controlling authority. We have, therefore, resolved to adopt substantial portions of the language of the *Panko* opinion as our own with appropriate additions and deletions. To avoid the necessity of a multitude of quotes and internal quotes, we simply here state that the substantive portions (as opposed to the statement of fact and disposition) of part I of this opinion, including footnotes, are quoted from the *Panko* decision except for ma erial enclosed in brackets,

including footnotes, which we have added. Deletions from quotations from the *Panko* opinion, other than the deletion of the name of Pan American and the substitution therefor of Fidelity Federal, will be indicated by ellipses or other appropriate designation.

I — THE MOORE CASE

A. The Facts

A fact common to all three cases is that Fidelity Federal is a private mutual savings and loan association chartered by the Federal Home Loan Bank Board pursuant to section 5(a) of the Home Owners' Loan Act of 1933 (12 U.S.C. §§1461-1470).

On February 22, 1978, Fidelity Federal made a loan of $58,800 to Paul M. and Debra J. Stitch secured by a deed of trust on their residential real property at 3109 Roosevelt Way, Costa Mesa, in the State of California. The deed of trust contained a due-on-sale clause purportedly giving Fidelity Federal the right to declare the unpaid balance of the loan immediately due and payable in the event the property was sold or otherwise transferred or conveyed by the borrowers.

The deed of trust also contained a provision identified as paragraph 15 stating that the deed of trust "shall be governed by the law of the jurisdiction in which the Property is located."[1]

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[1][In full the provision reads: "Uniform Deed of Trust; Governing Law; Severability. This form of deed of trust combines uniform covenants for national use and non-uniform covenants with limited variations by jurisdiction to constitute a uniform security instrument covering real property. This Deed of Trust shall be governed by the law of the jurisdiction in which the Property is located. In the event any provision or clause of this Deed of Trust or Note conflicts with applicable law, such conflicts shall not affect other provisions of this Deed of Trust or the Note which can be given effect without the conflicting provision, and to this end the provisions of t e Deed of Trust and the Note are declared to be severable."]

On September 15, 1978, the Stitches sold and, by grant deed, transferred the property to plaintiffs Alfonso Moore and Alice Moore.

Having learned that the property had been sold and conveyed to the Moores, Fidelity Federal gave notice of its intention to exercise the due-on-sale clause in the deed of trust and on December 7, 1978, caused to be recorded a notice of default and election to sell under the deed of trust. Whereupon, the Moores instituted this action.

B. Federal Preemption

Background

In recent years the validity of due-on-sale clauses has been a matter of considerable controversy in state and federal courts. In California our Supreme Court has determined that enforcement of a due-on-sale clause upon occurrence of an outright sale constitutes an unreasonable restraint on alienation "unless the lender can demonstrate that enforcement is reasonably necessary to protect against impairment to its security or the risk of default." (*Wellenkamp v. Bank of America, supra,* 21 Cal.3d at p. 953.) The court's decision was grounded on Civil Code section 711,[2] . . . [which, as interpreted, invalidates unreasonable restraints on the alienation of real property. (21 Cal.3d at p. 948.)]

Here, [Fidelity Federal makes no claim] . . . of an impairment to its security or risk of default as a result of the outright sale of the property to plaintiffs. Consequently, under California law the due-on-sale clause contained in the deed of trust herein would not be enforceable. [Fn. omitted.] [Fidelity Federal] . . . contends that it cannot be bound by California law since it is exclusively governed by regulations

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[2]Section 711 of the Civil Code provides: "Conditions restraining alienation, when repugnant to the interest created, are void."

of the Federal Home Loan Bank Board (Board) which preempt conflicting state laws.

In 1933 the Home Owners' Loan Act [HOLA] (12 U.S.C. §§1461-1470) was enacted by Congress . . . authorizing the establishment of federal savings and loan associations. While the associations are specifically empowered to extend real estate loans (12 U.S.C. §1464(c)(1)(B) and (c)(2)(A)), the statute is silent with respect to due-on-sale clauses or other loan details.

The Board [created in 1932 by th Federal Home Loan Bank Act (12 U.S.C. §§1421-1499)] is statutorily authorized to promulgate regulations[4] . . . ["to provide for the organization, incorporation, examination, operation, and regulation of" federal savings and loan associations. (12 U.S.C. §1464(a)(1).] [From 1933 to June 8, 1976, the Board's regulations were silent with respect to due-on-sale clauses.][12] The first specific mention of due-on-sale clauses, . . . [appears in] a regulation . . . enacted [June 8, 1976 and] . . . effective July 1, 1976, [purporting to restrict the exercise of due-on-sale clause in certain circumstances and] providing [in part] as follows: "An association *continues to have the power to include, as a matter of contract between*

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[4]"In order to provide local mutual thrift institutions in which people may invest their funds and in order to provide for the financing of homes, the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations', or 'Federal mutual savings banks' (but only in the case of institutions which, prior to conversion, were State mutual savings banks located in States which authorize the chartering of State mutual banks, provided such conversion is not in contravention of State law), and to issue charters therefor, giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States." (12 U.S.C. §1464.(a)(1).)

[12][However, the Board has interpreted a 1948 regulation calling for provisions in the loan contract "for full protection to the . . . association" as authorizing the use and automatic exercise of due-on-sale clauses and, indeed, as preemptin ; state law. (See discussion *infra*.)]

it and the borrower, a provision in its loan instrument whereby the association may, at its option, declare immediately due and payable sums secured by the association's security instrument if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent. Except as provided in paragraph (g) of this section [restricting exercise of due-on-sale clauses] with respect to loans made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, exercise by the association of such option (hereafter called a due-on-sale clause) *shall be exclusively governed by the terms of the loan contract*, and all rights and remedies of the association and borrower *shall be fixed and governed by that contract*" [Italics added.] (12 C.F.R. §545.6-11(f), amended and recodified at §545.8-3(f) (1980).)

The pivotal question to be decided is whether the federal regulation overrides state law embodied in California Civil Code section 711, as interpreted in *Wellenkamp*.

Federal Preemption

(1) The preemption doctrine arises under the supremacy clause of the federal constitution which states: "This Constitution, and the [L]aws of the United States which shall be made in [P]ursuant thereof; . . . shall be the supreme [L]aw of the [L]and; and the Judges in every State shall be bound thereby, any [T]hing in the Constitution or [L]aws of any State to the [C]ontrary notwithstanding." (U.S. Const., art. VI, cl. 2.) But the enumerated powers of the federal government are expressly limited: "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." (U.S. Const., Amend. X.) The United States Supreme Court has exhibited considerable

restraint in finding federal preemption of state law by requiring either "such actual conflict between the two schemes of regulation that both cannot stand in the same area, [or] . . . evidence of a congressional design to preempt the field." (*Florida Avocado Growers v. Paul* (1963) 373 U.S. 132, 141 [10 L.Ed.2d 248, 256, 83 S.Ct. 1210]; accord *People v. Conklin* (1974) 12 Cal.3d 259, 264 [114 Cal.Rptr. 241, 522 P.2d 1049], app. dism. 419 U.S. 1064 [42 L.Ed.2d 661, 95 S.Ct. 652].)

With reference to congressional intent, the United States Supreme Court has declared that a state regulation exercising the state's "historic police powers" is not displaced by federal law "unless that was the clear and manifest purpose of Congress." (*Jones v. Rath Packing Co.* (1977) 430 U.S. 519, 525 [51 L.Ed.2d 604, 613-614, 97 S.Ct. 1305]; *Rice v. Santa Fe Elevator Corp.* (1947) 331 U.S. 218, 230 [see also *New York Dept. of Social Services v. Dublino* (1973) 413 U.S. 405, 413-415 (37 L.Ed.2d 688, 695-696, 93 S.Ct. 2507)].) Counsel have not . . . [pointed out nor have we discovered] evidence of a clear congressional mandate that federal [rather than state] law shall control the . . . [determination as to whether the exercise within a state by a federally chartered savings and loan of a due-on-sale clause in the absence of any impairment or threat of impairment to its security is invalid as an unreasonable restraint on the alienation]. While the Congress [in HOLA] has unequivocally expressed its preemptive design in relation to specific areas of savings and loan association activities,[5] . . .

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[5]The Home Owners' Loan Act specifically provides that federal savings and loan associations are exempt from state limitations on the number of branch offices (12 U.S.C. §1464(a)(1), but are not exempt from more stringent state laws on neighborhood discrimination or consumer credit protection. (*Ibid.*) Further, federal savings and loan associations are exempt from state taxation greater than that imposed on local financing institutions. (*Id.*, at §1464(h).)

[HOLA] makes no reference to the subject of due-on-sale clauses.

[Invoking the somewhat discredited "occupation of the field" doctrine (see *Derenco, Inc. v. Benj. Franklin Fed. Sav. & Loan Ass'n* (1978) 281 Ore. 533 [577 P.2d 477, 484]; see also *New York Dept. of Social Services v. Dublino, supra*, 413 U.S. at pp. 413-415 [37 L.Ed.2d at pp. 695-696, 93 S.Ct. 2507]; see generally O'Connell, *The Due-On-Sale Clause in Florida: A Potential Battleground for Borrowers and Lenders* (1979) 31 Univ. of Fla. L.Rev. 933, 957-959), defendants emphasize the broad delegation of authority from Congress to the Board found in section 5(a) of HOLA (12 U.S.C. § 1464(a)(1)) to promulgate rules and regulations "to provide for the organization, incorporation, examination, operation and regulation of associations" (see fn. 4, *ante*). But this mistakes the plenary authority of the Board to regulate and control federal savings and loan associations (see *e.g., Conference of Federal Sav. & Loan Ass'ns v. Stein* (9th Cir. 1979) 604 F.2d 1256, 1257-1258, 1260, affd. (1980) 445 U.S. 921 [63 L.Ed.2d 754, 100 S.Ct. 1304]; *Kupiec v. Republic Federal Savings & Loan Ass'n* (7th Cir. 1975) 512 F.2d 147, 150; *Glendale Fed. Sav. & Loan Ass'n v. Fox* (C.D. Cal. 1978) 459 F.Supp. 903, 909, judgment entered (1979) 481 F.Supp. 616, app. pending 9th Cir.); *Rettig v. Arlington Hgts. Fed. Sav. & Loan Ass'n* (N.D.Ill. 1975) 405 F.Supp. 819, 823), which no one questions, with the intent of Congress to supplant the laws of all 50 states pertaining to real property and mortgages, areas of fundamental state concern traditionally governed exclusively by state law. (See, *e.g., State Land Bd. v. Corvallis Sand & Gravel Co.* (1977) 429 U.S. 363, 378-379 [50 L.Ed.2d 550, 563, 97 S.Ct. 582]; *United States v. Little Lake Misere L. Co.* (1973) 412 U.S. 580, 591-592 [37 L.Ed.2d 187, 1[illegible]6, 93 S.Ct. 2389].) It is one

thing to say that Congress has given the Board plenary authority to regulate federally chartered savings and loan associations. It is another thing entirely to say that by virtue of its federal charter, a federal savings and loan association is not required to abide by the state law of real property and mortgages in the state in which it does business.[3]

[Moreover, the occupation of the field argument overlooks both a fundamental problem that would exist were the argument accepted and the historical use of and compliance with the state law of real property and mortgages by federal savings and loan associations. When federal preemption is declared on the basis of "occuptation of the field," no state law pertaining to the "field" is applicable, whether or not it conflicts with the federal law. (*Meyers v. Beverly Hills Federal Savings & Loan Ass'n* (9th Cir. 1974) 499 F.2d 1145, 1146; *Glendale Fed. Sav. & Loan Ass'n v. Fox, supra*, 459 F.Supp. at p. 907; *Derenco, Inc. v. Benj. Franklin Fed. Sav. & Loan Ass'n, supra*, 577 P.2d at p. 484.) But federal savings and loan associations have always used and been governed by state real property and mortgage law in respect to such matters as title, conveyancing, recording, priority of liens, proceedings for foreclosure, and deficiency judgments. (See, *e.g.*, *In re Wilton-Maxfield Management Co.* (9th Cir. 1941) 117 F.2d 913 [antideficiency statute]; *Federal National Mortgage Association v. Kostrunek* (S.D. Iowa 1964) 228 F.Supp. 777 [methods of foreclosure and right of redemption]; *Tahoe Highlander v. Westside Fed. Sav. & L.* (1979) 95 Nev. 8 [588 P.2d 1022] [antideficiency

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[3][Usually federal savings and loan associations do business wholly within one state. (See 12 C.F.R. § 545.6-6, amended and recodified as §545.8-6.) There are about 10 savings and loan associations which, by reason of their preexisting status upon conversion, have branches outside their home state. (Hearing before the House Com. on Banking, Fianance and Urban Affairs on H.R. No. 3864, 96th Cong., 1st Sess., at p. 163 (1979).)

law]; *Benj. Franklin Federal S. & L. Ass'n v. Almond* (1978) 282 Ore. 303 [577 P.2d 937] [prior decree no bar to foreclosure suit]; *Caudle v. First Federal Sav. & L. Ass'n of Sylacauga* (1976) 295 Ala. 409 [327 So.2d 911] [statutory right of redemption]; *Minn. Fed. Sav. v. Cent. Enter. of Superior* (1976) 311 Minn. 46 [247 N.W.2d 46]; *Hartford Federal Savings and Loan Ass'n v. Lenczyk* (1966) 153 Conn. 457 [217 A.2d 694] [antideficiency law]; *Apex Siding & Roof Co. v. First Federal Sav. & L. Ass'n* (Okla. 1956) 301 P.2d 352 [equitable estoppel to assert priority]; *Anatole Caron, Inc. v. Manchester Federal Sav. & L. Ass'n* (1940) 90 N.H. 560 [10 A.2d 668] [mechanic's lien law]; *First Federal Savings & L. Ass'n of Martin Cty. v. Ott* (Fla.App. 1973) 285 So.2d 695, cert. den. (Fla. 1974) 291 So.2d 10 [constructive notice]; *Home Fed. Sav. & L. Ass'n v. Four Star Heights, Inc.* (1971) 70 Mis.2d 118 [333 N.Y.S.2d 334] [mechanic's lien law]; *Penn Federal Savings and Loan Ass'n v. Joyce* (1962) N.J.Super. 275 [183 A.2d 114] [statutory and equitable rights of redemption]; *Kankakee Federal Sav. & L. Ass'n v. Arnove* (1943) 318 Ill.App. 261 [47 N.E.2d 874] [priority and subordination agreement]; *First Fed. Sav. & L. Ass'n v. Green-Acres Bldg. Corp.* (1963) 38 Misc.2d 149 [236 N.Y.S.2d 1009] [priority of lien under future advances clause].) In the event of a foreclosure, a federal savings and loan association would undoubtedly also be subject to state law in obtaining possession of the property. And it can hardly be otherwise, for there is no federal common law of mortgages or real property. (See *Kirkland v. Fidelity Federal Sav. & Loan Ass'n of Jacksonville* (D.Fla. 1980) ____ F.Supp. ____, ____; see also *Hoopeston Co. v. Cullen* (1943) 318 U.S. 313, 318 [87 L.Ed. 777, 783, 63 S.Ct. 602, 145 A.L.R. 1113].)

[The *Wellenkamp* decision, of course, was based on California Civil Code section 711, the source of California law

on the validity of restraints against alienation of real property (see *Wellenkamp v. Bank of America, supra*, 21 Cal.3d at pp. 948, 949; *Coast Bank v. Minderhout* (1964) 61 Cal.2d 311, 316 [38 Cal.Rptr. 505, 392 P.2d 265], overruled to the extent inconsistent on another point in *Wellenkamp v. Bank of America, supra*, 21 Cal.3d at p. 953), and is part of the California law of real property and mortgages.

[We consider next the contention that the Board in its regulations and rulings has expressly preempted application of the state law.

[Notwithstanding that its regulations had not theretofore mentioned due-on-sale clauses, on July 30, 1975, by resolution number 75-647 in the form of an advisory opinion rendered at the request of the court in a case entitled *Eric R. Schott, et al. v. Mission Federal Savings and Loan Association, et al.* in the United States District Court for the Central District of California (case No. CIV-75-366 WMB) the Board interpreted the "full protection" language in a regulation in effect since 1948 "as authorizing 'due-on-sale' clauses for Federal associations (regardless of any State law to the contrary) because, . . . such clauses 'provide for full protection to the Federal association.' " (Advisory opinion, p. 15.) As stated by the Supreme Court of Minnesota in its opinion filed April 3, 1981, in *Holiday Acres v. Midwest Fed. Sav. & Loan Ass'n.*: "We reject [defendants'] argument that state regulation of the exercise of due-on-sale clauses was preempted prior to 1976 by [the] regulation which states, 'Loan instruments shall . . . provide for full protection to the Federal association.' 12 C.F.R. §545.8-3(a). This language, in the context of the regulation cited, refers to insurance, taxes, assessments, repairs, and other factors enumerated in that section." (___ Minn. ___ [___

N.W.2d ____, ____])[4] Moreover, there is no conflict whatever between the "full protection" regulation and the California law. California law does not invalidate all exrcises of due-on-sale clauses; only unreasonable restraints on alienation are held invalid (*Wellenkamp v. Bank of America, supra*, 21 Cal.3d at p. 948; *La Sala v. American Sav. & Loan Assn* (1971) 5 Cal.3d 864, 878-879 [97 Cal.Rptr. 849, 489 P.2d 1113]); the exercise of a due-on-sale clause is permitted when "the lender can demonstrate that enforcement is reasonably necessary to protect against impairment to its security or the risk of default." (*Wellenkamp v. Bank of America, supra*, 21 Cal. 3d at p. 953, fn. omitted.)

[While involved in litigation with officials of the State of California concerning the exercise by federal savings and loan associations of due-on-sale clauses, the Board on June 8, 1976, promulgated its due-on-sale clause regulation. (12 C.F.R. §545.6-11(f), amended and recodified as §545.8-3(f) (1980)) (See text following fn. [2], *ante*.) Although the regulation itself expressly states that "exercise by the association of such option (hereafter called a due-on-sale clause) shall be exclusively governed by the terms of the loan contract, and all rights and remedies of the association and borrower shall be fixed and governed by that contract," in a preamble accompanying the regulation the Board stated:

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[4][12 C.F.R. §545.6-11, amended and recodified as §545.8-3 (1980), reads in pertinent part: "(a) *Required and authorized provisions.* Each loan shall be evidenced by note, bond or other instrument and be secured by a security instrument which is consistent with sound lending practices. Loan instruments shall comply with applicable provisions of law, governmental rules and regulations, and the association's charter and bylaws, and provide for full protection to the Federal association. They shall be recorded and, among other protections, *shall provide specifically for full protection with respect to insurance, taxes, assessments, other governmental levies, maintenance, and repairs.* They may provide for an assignment of rents. *The association may pay taxes, assessments, insurance premiums, and other similar charges for protection of its interest in the security property.* . . ." (Italics added.)]

"Finally, it was and is the Board's intent to have . . . due-on-sale practices of Federal associations governed exclusively by Federal law. Therefore, . . . exercise of due-on-sale clauses by Federal associations shall be governed and controlled solely by §545.6-11 and the Board's new Statement of Policy. Federal associations shall not be bound by or subject to any conflicting State law which imposes different . . . due-on-sale requirements, nor shall Federal associations attempt to . . . avoid the limitations on the exercise of due-on-sale clauses delineated in §545.6-11(g) on the ground that such . . . avoidance of limitations is permissible under State law." (Preamble to 12 C.F.R. §545.6-11, 41 Fed. Reg. 18287 (May 3, 1976).)]

[Thus it] is clear that the *Board* has manifested *its* unqualified intention that the adopted regulations and implementing policy relating to due-on-sale clauses shall occupy a preemptive position over conflicting state law provisions. [Italics added; fn. omitted.] Such expression of administrative intent was found controlling in *Glendale Fed. Sav. & Loan Ass'n v. Fox*, [*supra*, 459 F.Supp. at pp. 909-910)]. But we cannot equate the *Board's* expression of intent with the requisite *congressional* intent [italics added] since the ultimate question to be answered is "whether *Congress* has . . . ordained that the state regulation shall yield." (*Florida Avocado Growers v. Paul, supra*, 373 U.S. at p. 146 [10 L.Ed.2d at p. 259]; italics added; [accord: *New York Dept. of Social Services v. Dublino, supra*, 413 U.S. at pp. 413-418 [37 L.Ed.2d at pp. 695-697]; *Katherine Gibbs Sch. (Inc.) v. F.T.C.* (2nd Cir. 1979) 612 F.2d 658, 667, rehg. den. 628 F.2d 755].) [The decision whether to displace state law is a fundamental one going to the very fabric of federalism; thus, the decision is one to be made by the people through their elected representatives in Congress rather than by agencies or tribunals insulated from democratic pres-

sures. (Cf. *City of Milwaukee v. Illinois*, (April 28, 1981)* ___ U.S. ___, ___, [___ L.Ed.2d ___, ___, ___ S.Ct. ___]; *Katherine Gibbs Sch. (Inc.) v. F.T.C., supra.*)]

But despite the lack of express congressional design, federal law by implication may operate to the exclusion of state law "where compliance with both federal and state regulations is a physical impossibility" or where there is an "impossibility of dual compliance . . . resulting in . . . (an inevitable collision between the two schemes of regulation, . . ." (*Florida Avocado Growers v. Paul, supra*, 373 U.S. at pp. 142-143 [10 L.Ed.2d at p. 257].)

In an early case a federal district court—confronted with the question whether a federally chartered savings and loan association was required to obtain a state certificate to transact business in the state—held in favor of federal preemption reasoning that: "The [Home Loan Bank] Board has adopted comprehensive rules and regulations concerning the powers and operations of every Federal savings and loan association from its cradle to its corporate grave." (*People, etc. v. Coast Federal Sav. & Loan Ass'n* (S.D.Cal. 1951) 98 F.Supp. 311, 316.) This broad declaration of lifetime supremacy has been cited with approval in a number of subsequent decisions uniformly holding that state law may not regulate [federal savings and loan associations] or otherwise interfere with . . . [their] internal affairs. . . . (See e.g., *Conference of Federal Sav. & Loan Ass'ns v. Stein* [*supra*] 604 F.2d 1256, . . . [proceedings for credit discrimination]; *Kupiec v. Republic Federal Savings & Loan Ass'n* [*supra*] 512 F.2d [at p.] 150 [use of membership records]; *Meyers v. Beverly Hills Federal Savings & Loan Ass'n* [*supra*] 499 F.2d [at p.] 1147 [prepayment penalties]; *Rettig v. Arlington Hghts. Fed. Sav. & Loan Ass'n* [*supra*] 405 F.Supp. [at p.]

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823 [fiduciary obligations of directors and officers]; *City Federal Savings & Loan Ass'n v. Crowley* (E.D. Wisc. 1975) 393 F.Supp. 644, 655 [fees received by directors and officers]; *Kaski v. First Fed. S & L Ass'n of Madison* (1976) 72 Wisc.2d 132 [240 N.W.2d 367] [interest rate escalation]; *Sears v. First Federal Savings and L. Ass'n of Chicago* (1971) 1 Ill.App.3d 621 [275 N.E.2d 300] [trust accounts for taxes and insurance]; see also *Derenco, Inc. v. Benj. Franklin Fed. Sav. & Loan Ass'n* [*supra*] 281 Or. 533 [577 P.2d 477], cert. den. 439 U.S. 1051 [58 L.Ed.2d 712, 99 S.Ct. 733].) [Bracketed descriptions in the original.]

Although that general proposition reflects a correct statement of law, we are not persuaded that existing state law pertaining to the exercise of due-on-sale clauses in any way infringes upon or is otherwise incompatible with the Board's regulation or . . . [control] of . . . federal savings and loan associations. (See *Holiday Acres v. Midwest Fed. Sav. & Loan Ass'n* (Apr. 3, 1981, No. 338) ___ Minn. ___ [___ N.W.2d ____].) [Every substantive rule of state property and mortgage law has the potential for impinging upon federal savings and loan associations, but they are not thereby invalidated as "regulations" of the associations. As previously observed, the *Wellenkamp* rule is a substantive rule of California property and mortgage law. It is not directed at "regulating" and it is not a "regulation" of savings and loan associations as were the state law or state actions in *Conference of Federal Sav. & Loan Ass'ns v. Stein, supra*, 604 F.2d 1256, and *Glendale Fed. Sav. & Loan Ass'n v. Fox, supra*, 459 F.Supp. 903.]

[¶] The federal regulation merely authorizes and does not compel savings and loan associations to include a due-on-sale clause in their loan contracts and to exercise their rights thereunder. (*Holiday Acres v. Midwest Fed. Sav. & Loan Ass'n, supra.*) [P. 333.] As noted, California law

. . . [permits enforcement of] a due-on-sale clause only upon a showing that the lender's security will be either impaired or subjected to risk of default as a consequence of the transfer. But the federal loan association is not faced with physical impossibility in complying with the two regulatory schemes. Instead, the federal regulation leaves the rights and remedies of the parties intact under the terms of the loan contract. Thus, enforcement of the due-on-sale clause rests upon conventional contract and property principles under state law. (*Id.* at p. 10.) There is no "inevitable collision" between the two regulations. (*Florida Avocado Growers v. Paul, supra*, at p. 143 [10 L.Ed.2d at p. 257] [cf. *Derenco, Inc. v. Benj. Franklin Fed. Sav. & Loan Ass'n, supra*, 577 P.2d at pp. 483-484].)

The Federal Home Loan Mortgage Corporation (FHLMC), appearing as amicus curiae, urges a finding of federal preemption based on a claim of need for national uniformity of loan practices and instruments.[7] In response, we rely upon the persuasive language of the Minnesota Supreme Court: "If this national interest were indeed an important policy, it seems that the inclusion of such clauses would be mandated rather than permitted." (*Holiday Acres v. Midwest Fed. Sav. & Loan Ass'n, supra*, p. 338.) Nor, we think, would application of state law to the exercise of due-on-sale clauses interfere with the federal objectives embodied in the Home Owners' Loan Act. That legislation was

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[7]Briefly stated, the argument is made that due-on-sale clauses, by keeping the life of a mortgage relatively short, increase the lenders' yield and thereby promote the national interest by keeping overall interest rates down. Further, by providing a higher yield and a rapid return of capital to the lenders, due-on-sale clauses render the loans marketable in the secondary mortgage market, thereby attracting new funds to the mortgage market and, in turn, again keeping interest rates down. FHLMC, as purchaser of conventional mortgages, will purchase only those mortgages using the standardized FHLMC/FNMA loan instrument employed here.

enacted during a period of severe economic depression in order to assist financially distressed homeowners. It would be "unreasonable, and ironic, to hold now that the Congress intended [the act] to justify the removal of homeowners' protections under state law." (*Id.* at p. 339.)

Our conclusion finds further support in the particular provisions of the deed of trust employed herein. The form of instrument is apparently one promulgated by the FHLMC itself; its use is a precondition to purchase of the mortgage by FHLMC. The trust instrument contains so-called "uniform" and "non-uniform" covenants. The uniform covenants are intended for nationwide use while the non-uniform covenants are tailored to particular state mortgage requirements. [Fn. omitted.] For example, the "nonuniform" covenants employed herein include California statutory requirements regarding notice (Civ. Code, § [2924b]) reinstatement (Civ. Code, § [2924c]) and the furnishing of a statement of obligation (Civ. Code, § 2943.)

Included in the "uniform" covenants found in paragraph 15 [of the deed of trust] is the express proviso that: "[This form of deed of trust combines uniform covenants for national use and non-uniform covenants with limited variations by *jurisdiction* . . . .] *This Deed of Trust shall be governed by the law of the jurisdiction in which the Property is located.* In the event that any provision or clause of this Deed of Trust or Note *conflicts with applicable law* [italics added], such conflict shall not affect other provisions . . . ." (Italics added.) We believe such language expresses an unmistakable intention that state law shall govern the interpretation, validity and enforcement of the loan-security instrument.

[Defendants and amicus Federal Home Loan Mortgage Corporation contend that the law of a state includes all federal law the state is required to enforce, by preemption

or otherwise, so that the provision in paragraph 15 that the deed of trust shall be governed by the law of the jurisdiction in which the property is located has reference to both the state and federal law enforceable in that jurisdiction and that, inasmuch as the state law of California in respect to the exercise of due-on-sale clauses is preempted by the Board's regulation, the paragraph 15 provision is of no real significance in this case. Not so.

[Of course, reference to state law in some contexts may include reference to the federal law enforceable in the state, but to accept that interpretation here would entirely overlook the next sentence in paragraph 15 referring to a possible conflict of provisions or clauses of the deed of trust "with applicable law." If defendants and amicus were said to be correct that state law has been preempted by federal occupation of the field, there would be no "applicable law" other than the federal law and therefore no provision or clause of the deed of trust could be in conflict "with [the] applicable law." The same nonsensical result would flow from a holding that the "full protection" regulation preempts state law. Virtually every clause and provision in the deed of trust is for the "protection" of the association, and if state law were as a consequence preempted, there would be no "applicable law" with which any such clause or provision could be in conflict.

[Thus, we are confirmed in our conclusion that paragraph 15 means just what it seems to say, that the law of California governs the validity and interpretation of deeds of trust on California Property. Even if the matter were in doubt, the meaning of the provision would at least be ambiguous and uncertain, and the ambiguity and uncertainty would be construed against Fidelity Federal, the party responsible for it. (Civ. Code, §1654; *Hibernia Sav. & Loan Soc. v. Lauffer* (1940) 41 Cal.App.2d 725, 731 [107 Cal.Rptr. 494]; *Bi-*

tuminous Casualty Corporation v. Lynn (6th Cir. 1974) 503 F.2d 636, 640-641; *Kenneth Reed Construction Corp. v. United States* (1973) 475 F.2d 583, 588 [201 Ct.Cl. 282].)]

In conclusion, we hold that California law is not preempted by virtue of the relevant federal regulation.

C. Disposition

As to the Moore case (Super. Ct. No. 306349), the judgment is reversed with directions to render summary judgment in favor of the plaintiffs.

II — THE WHITCOMBE CASE

A. The Facts

On July 17, 1972, Fidelity Federal made a loan of $29,200 to Carter and Irene R. Wood secured by a deed of trust on their residential real property at 7392 Natal Drive, Westminster, in the State of California. The deed of trust contained a due-on-sale clause purportedly giving Fidelity Federal the right to declare the unpaid balance of the loan immediately due and payable in the event the property was sold or otherwise transferred or conveyed by the borrowers. The deed of trust also contained a provision stating that the deed of trust "shall be governed by the law of the jurisdiction in which the Property is located." (See full text of the provision set forth in bracketed fn. 1, *ante*.)

On November 9, 1978, the Woods sold and, by grant deed, transferred the property to plaintiff John D. Whitcombe.

Having learned that the property had been sold and conveyed to Whitcombe, Fidelity Federal gave notice of its intention to exercise the due-on-sale clause in the deed of trust and on December 29, 1978, caused to be recorded a notice of default and election to sell under the deed of trust. Whereupon, Whitcombe instituted suit.

B. Federal Preemption

The principles discussed under the heading "Federal Preemption" in the Moore cases are fully applicable to this case. In fact, they apply a fortiori here, because the deed of trust in this case was executed July 17, 1972, years before the Board's promulgation of its due-on-sale regulation on June 8, 1976, which expressly indicates that it is not applicable to security instruments executed prior to that date. As indicated in our discussion of the preemption issue in the Moore case, the contention that state law was theretofore preempted by the "full protection" regulation is devoid of merit.

Accordingly, we hereby incorporate as though fully set forth our discussion of the federal preemption issue in section IB of this opinion, and we conclude that the *Wellenkamp* rule is applicable.

C. Disposition

As to the Whitcombe case (Super. Ct. No. 308527), the judgment is reversed with directions to render summary judgment in favor of the plaintiff.

III — THE DE LA CUESTA CASE

A. Facts

On January 18, 1971, Fidelity Federal made a loan of $105,000 to Howard G. and Ellen Mae Trabant secured by a deed of trust on what we are told is commercial property at 19462-19488 Beach Boulevard, Huntington Beach, in the State of California. The deed of trust contained a due-on-sale clause purportedly giving Fidelity Federal the right to declare the unpaid balance of the loan immediately due and payable in the event the property was sold or otherwise transferred or conveyed by the borrowers.

On October 25, 1977, the Trabants sold and, by grant deed, transferred the property to plaintiffs Reginald de la Cuesta and Margaret de la Cuesta.

Having learned that the property had been sold and conveyed to the de la Cuestas, Fidelity Federal gave notice of its intention to exercise the due-on-sale clause in the deed of trust and on December 7, 1978, caused to be recorded a notice of default and election to sell under the deed of trust. Whereupon, the de la Cuestas instituted this action.

B. Federal Preemption

The principles set forth in our discussion of federal preemption in the Moore case are fully applicable to this case also. In fact, again, they apply a fortiori in this case because the Trabant deed of trust was executed January 18, 1971, many years prior to promulgation by the Board of its due-on-sale regulation on June 8, 1976, and, as indicated in our discussion in the Moore case, the contention that state law was theretofore preempted by the "full protection" regulation is devoid of merit.

We recognize that the deed of trust here involved does not contain a provision such as that found in the other two deeds of trust to the effect that it shall be governed by the law of the jurisdiction in which the property is situated. However, our conclusion in the Moore case was not based so much on an agreement between the parties for the application of state law as on the conclusion that the general use of a provision containing such language by federal savings and loan associations with the approval of the Board persuasively evidences a recognition by the Board and federal savings and loan associations that state law would govern the interpretation, validity and enforcement of security instruments. Thus, the absence of the special provision in

the particular trust deed, here, is of no great significance to our resolution of the preemption issue.

Accordingly, with the exception of those portions relating directly to the special provision in the Moore deed of trust, we hereby incorporate as though fully set forth our discussion of the preemption issue under section IB of this opinion and conclude that application of the state law has not been federally preempted.

C. The Commercial Property Problem

(2) There is nothing in the pleadings and virtually nothing in the declarations in support of the motions for summary judgment that discloses the precise nature of the property encumbered by the deed of trust in this case. One document indicates that it is "commercial" and "income producing." Otherwise we are in the dark.

Defendants assert that there are a number of differences between owner-occupied residential property and income-producing, commercial property from which defendants conclude that the rule in *Wellenkamp* ought not to be applied to a deed of trust on commercial property. They assert that owners of commercial property have the ability to raise rents or prices of manufactured goods; that an owner of commercial property is less likely than a homeowner to be compelled to transfer the property at a time of "tight" money; that buyers of commercial property are not normally compelled to purchase at a time of "tight" money; and that commercial buyers carefully weigh business and tax advantages, whereas residential buyers do not.

We are aware, of course, that in *Holiday Acres v. Midwest Fed. Sav. & Loan Ass'n, supra*, ___ N.W.2d ___ at page ___, the Minnesota Supreme Court was impressed with some such differences in concluding that automatic exercise of a due-on-sale clause in a security instrument used to

finance residential investment property was not impermissible. However, the declarations in support of the motions for summary judgment in the case at bench contain no competent evidence to establish the factual distinctions asserted by defendants, and we are unable and unwilling to take judicial notice of them. Moreover, it seems to us that at least the last of the differences asserted by defendants argues as well for application of the *Wellenkamp* rule as against its application.

Defendants also call to our attention that the property involved in *Wellenkamp* was apparently not commercial property and that the court in the *Wellenkamp* decision mentioned the preferred status under California law of a homeowner's equity. (21 Cal.3d at p. 950, fn. 6.) That is true, but the *Wellenkamp* court did not even specifically mention that the property in that case was residential, much less differentiate in its language between commercial and residential properties. The court consistently used generic phraseology such as "a parcel of real property," "real property" and "real estate loans." (See, *e.g.*, 21 Cal.3d at pp. 946, 947, 949, 950, 951, 953 and 954.)

The basis for decision was that exercise of a due-on-sale clause in the absence of any threat of impairment to the security or risk of default resulting from the sale or transfer constitutes an unreasonable restraint on alienation. Going to the heart of the decision was the following language of the court: "Economic risks such as those caused by an inflationary economy are among the general risks inherent in every lending transaction. They are neither unforeseeable nor unforeseen. Lenders who provide funds for long-term real estate loans should and do, as a matter of business necessity, take into account their projections of future economic conditions when they initially determine the rate of payment and the interest on these long-term loans. [Cita-

tion.] Unfortunately, these projections occasionally prove to be inaccurate. We believe, however, that it would be unjust to place the burden of the lender's mistaken economic projections on property owners exercising their right to freely alienate their property through the automatic enforcement of a due-on-sale clause by the lender." (*Id.*, at pp. 952-953, fn. omitted.) There is no suggestion in the court's language that its reasoning would have been different had the encumbered property been commercial rather than residential property. We also note that *Tucker v. Lassen Sav. & Loan Assn.* (1974) 12 Cal.3d 629 [116 Cal.Rptr. 633, 526 P.2d 1169], upon which the *Wellenkamp* court heavily relied, involved a house used as residential investment property. (*Id.*, at p. 633.)

In fine, if there are circumstances in which the *Wellenkamp* rule should not be applied because of the commercial nature of the encumbered property, they have not been made to appear in this case, and we see no reason the *Wellenkamp* rule should be inapplicable in the circumstances here shown.

D. Disposition

As to the de la Cuesta case (Super. Ct. No. 286474) the judgment is reversed with directions to the trial court to enter summary judgment in favor of the plaintiffs.

McDaniel, J., and Morris, J., concurred.

Trial Court Order Granting Summary Judgment

[Filed October 18, 1979]

Superior Court of the State of California for the County of Orange.

DEAN L. GROSS, PEDRO ENRIQUEZ, Plaintiffs, v. GLENDALE FEDERAL SAVINGS AND LOAN ASSOCIATION, VERDUGO SERVICE CORPORATION, and DOES I through XX, inclusive, Defendants; GLENDALE FEDERAL SAVINGS AND LOAN ASSOCIATION, Cross-Complainant, v. DEAN L. GROSS and PEDRO ENRIQUEZ, Cross-Defendants; Case No. 315345.

This cause came to be heard by the Court upon the motion of defendants Glendale Federal Savings and Loan Association and Verdugo Service Corporation for specification of issues without substantial controversy and dismissal of plaintiffs' Complaint For Declaratory Relief, Attorneys' Fees, Injunction and Slander of Title as against such defendants. At the hearing on defendants' motion, held on October 17, 1979, plaintiffs were represented by John W. Dumas and defendants were represented by Terry A. Fralich of the law firm of McKenna & Fitting.

The Court was presented with and received evidence, considered the papers filed by the parties, the proceedings had and taken herein and the arguments made by the parties, and was fully advised in the premises. In accordance therewith and good cause appearing therefor,

IT IS HEREBY FURTHER ORDERED AND ADJUDGED that the motion of defendants and cross-complainant Glendale Federal Savings and Loan Association and Verdugo Service Corporation for specification of issues without substantial controversy and for dismissal of plaintiffs' Complaint For Declaratory Relief, Injunction and Slander of Title herein is granted in all respects and that said Complaint against such defendants, and each of them,

shall be and hereby is dismissed with prejudice for failure to state a claim upon which relief can be granted.

DATED: October 18, 1979

EDWARD J. WALLIN
Edward J. Wallin
Superior Court Judge

APPROVED AS TO FORM:
By /s/ John W. Dumas
Attorney for Plaintiffs
Date: October 18, 1979

Trial Court Judgment

[Filed January 2, 1980]

In the Superior Court of the State of California for the County of Orange.

DEAN L. GROSS, PEDRO ENRIQUEZ, Plaintiffs, v. GLENDALE FEDERAL SAVINGS AND LOAN ASSOCIATION, VERDUGO SERVICE CORPORATION and DOES I through XX, inclusive, Defendants; GLENDALE FEDERAL SAVINGS AND LOAN ASSOCIATION, Cross-Complainant, v. DEAN L. GROSS and PEDRO ENRIQUEZ, Cross-Defendants; Case No. 315345.

This court having issued its Order, dated October 18, 1979, granting in all respects the motion of defendants and cross-complainant Glendale Federal Savings and Loan Association and Verdugo Service Corporation for specification of issues without substantial controversy and dismissal of plaintiffs' Complaint For Declaratory Relief, Slander Of Title, Cancellation of Instrument and Injunction as against such defendants; the Cross-Complaint For Damages of cross-complainant Glendale Federal Savings and Loan Association having been dismissed without prejudice by the Court pursuant to the request of such cross-complaint,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, that judgment be entered in favor of defendants. Federal law, including specifically 12 C.F.R. §545.6-11(f) and (g) (since renumbered as 12 C.F.R. §545.8-3(f) and (g)), exclusively governs the validity and exercisability of due-on-sale clauses in the loan instruments of federally-chartered savings and loan associations executed on or after

June 8, 1976. California law on the validity and exercisability of due-on-sale clauses does not apply to such loan instruments.

DATE: December 31, 1979.

EDWARD J. WALLIN
EDWARD J. WALLIN
Superior Court Judge

APPROVED AS TO FORM:

/s/ By John W. Dumas
John W. Dumas
Attorney for Plaintiffs

Date: December 13, 1979

McKENNA & FITTING

/s/ By Terry A. Fralich
Terry A. Fralich
Attorneys for Defendants

Date: December 7, 1979

California Supreme Court Denial of Hearing

CLERK'S OFFICE, SUPREME COURT, 4250 State Building, San Francisco, California 94102, September 16, 1981.

I have this day filed Order, Hearing Denied.

In re: 4 Civ. No. 21903, Gross vs. Glendale Federal Savings.

Respectfully, Clerk

Notice of Appeal

[Filed October 21, 1981]

Court of Appeal of the State of California, Fourth Appellate District, Division Two.

Dean L. Gross, et al., Plaintiffs and Appellants, vs. Glendale Federal Savings and Loan Association, et al., Defendants and Respondents, 4th Civil No. 21903.

NOTICE OF APPEAL TO UNITED STATES SUPREME COURT.

Notice is hereby given that Defendants and Respondents Glendale Federal Savings and Loan Association and Verdugo Service Corporation, and each of them, hereby appeal to the United States Supreme Court from the judgment of this Court entered July 23, 1981, in the within appeal. The California Supreme Court denied a timely Petition for Hearing with respect to this judgment on September 16, 1981.

The within appeal is taken under 28 U.S.C. §1257(1) and 28 U.S.C. §1257(2).

28 U.S.C. §2403(a) and 28 U.S.C. §2403(b) may be applicable to the within appeal.

Dated: October 21, 1981

McKENNA, CONNER & CUNEO
AARON M. PECK
TERRY A. FRALICH
C. STEVEN McMURRY

By /s/ Aaron M. Peck
Aaron M. Peck

Attorneys for Glendale Federal Savings and Loan Association and Verdugo Service Corporation

DECLARATION OF SERVICE

I, the undersigned, say:

I am a citizen of the United States and a resident of the Los Angeles County, California; I am over the age of eighteen years and not a party to the within entitled action; my business address is Twenty-Eighth Floor, 3435 Wilshire Boulevard, Los Angeles, California 90010.

On October 21, 1981, I served the within "Notice of Appeal to United States Supreme Court" by placing true copies thereof enclosed in sealed envelopes with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

John H. Dumas, Esq.
Suite 201
611 Civic Center Drive West
Santa Ana, California 92701

George Deukmejian, Attorney General
Arthur C. de Goede, Assistant Attorney General
Joseph M. O'Heron, Deputy Attorney General
3580 Wilshire Boulevard
Los Angeles, California 90010

Supreme Court of the State of California
4250 State Building
350 McAllister Street
San Francisco, California 94102

Solicitor General
Department of Justice
Washington, D. C. 20530

Federal Home Loan Bank Board
Office of General Counsel
1700 "G" Street, N. W.
Washington, D. C. 20552

Orange County Superior Court
700 Civic Center Drive West
Santa Ana, California 92701

I declare under penalty of perjury that the foregoing is true and correct.

EXECUTED on October 21, 1981, at Los Angeles, California.

Victoria C.M. Dimond

Article I, Section 8, Clause 3 of the United States Constitution ("The Commerce Clause")

"[Congress shall have Power] to regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes".

Article VI, Clause 2 of the United States Constitution ("The Supremacy Clause")

"This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding."

Section 5(a) of the Home Owners' Loan Act of 1933, 12 U.S.C. §1464(a):

As originally enacted:

"In order to provide local mutual thrift institutions in which people may invest their funds and in order to provide for the financing of homes, the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations', and to issue charters therefor, giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States." (Home Owners' Loan Act, ch. 64, §5(a), 48 Stat. 132 (1933).)

In its present form:

"(1) In order to provide local mutual thrift institutions in which people may invest their funds and in order to provide for the financing of homes, the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations,' or 'Federal mutual savings banks' (but only in the case of institutions which, prior to conversion, were State mutual savings banks located in States which authorize the chartering of State mutual savings banks, provided such conversion is not in contravention of State law), and to issue charters therefor, giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States. An association which was formerly organized as a savings bank under State law may not convert from the mutual to the stock form of ownership. An association which was formerly organized as a sav-

ings bank under State law may not convert from the mutual to the stock form of ownership. An association which was formally organized as a savings bank under State law may, to the extent authorized by the Board, continue to carry on any activities it was engaged in on December 31, 1977, and to retain or make any investments of a type it held on that date, except that its equity, corporate bond, and consumer loan investments may not exceed the average ratio of such investments to total assets for the five-year period immediately preceding the filing of an application for conversion and such an association which was formerly organized as a savings bank under State law shall only be permitted to establish branch offices and other facilities in accordance with the limitations imposed by State law controlling applications of a savings bank organized under such State law, provided that such an association: (A) shall be exempt from any numerical limitations of State law on the establishment of branch offices and other facilities, and (B) may, in any case, subject to the approval of the Board, establish branch offices and other facilities in its own Standard Metropolitan Statistical Area, its own county or within thirty-five miles of its home office, but only in its State of domicile. An association which was formerly organized as a savings bank under State law shall be subject to the requirements of State law (including any regulations promulgated thereunder and any sanction of the violation of any such law or regulation) in effect at the time of conversion, in the State of its original charter —

(A) pertaining to discrimination in the extension of home mortgage loans or adjustment in the terms of mortgage instruments based on neighborhood or geographical area,

(B) pertaining to requirements imposed under the Consumer Credit Protection Act,

if the Board determines that State law and regulations impose more stringent requirements than Federal law and regulations.

(2) A Federal mutual savings bank may make commercial, corporate, and business loans except that —

(A) not more than 5 per centum of the assets of such a bank may be so loaned; and

(B) such loans may only be made within the State where the bank is located or within 75 miles of the bank's home office.

(3) In addition to the authority conferred by paragraph (1), Federal mutual savings bank may accept demand deposits in connection with a commercial, corporate, or business loan relationship." (12 U.S.C.A. §1464(a) (1980).)

Federal Home Loan Bank Board Resolution No. 76-100

[41 Fed. Reg. 6283 (1976)]

[in pertinent part]

FEDERAL SAVINGS AND LOAN SYSTEM

LATE CHARGES AND DUE ON SALE CLAUSES

February 6, 1976.

The following summary of the amendment proposed by this Resolution is provided for the reader's convenience and is subject to the full explanation in the following preamble and to the specific provisions of the proposed amendment.

I. *Present situation.* The Federal Home Loan Bank Board permits Federal associations, if authorized by their loan contracts, to assess, impose, and collect late charges respecting delinquent periodic installment payments on such loans, and to declare the loan immediately due and payable if the borrower sells or transfers the real property securing the loan without the consent of the association.

II. *Proposed Regulation.* A. Would continue to empower a Federal association to include, as a matter of contract between it and the borrower, provisions in its loan contracts for assessment, imposition, and collection of a late charge respecting any delinquent periodic installment payment on the loans, and for the acceleration of the maturity of the loan, at the option of the association, if the borrower sells or transfers the loan security property without the prior written consent of the association.

B. Would place specified limits on the maximum amount of late charges which could be collected by a Federal association on future contracts as to loans on the security of a home (1-4 family) occupied or to be occupied by the borrower.

C. Would restrict the circumstances under which a Federal association could exercise its acceleration option (due

on sale clause) on future contracts as to loans on the security of a home (1-4 family) occupied or to be occupied by the borrower.

III. *Reasons for Proposed Change*. A. To clarify the existing authority of Federal associations to assess, impose, and collect late charges, and to set limits on late charges which can be collected by Federal associations on future loans on the security of a home occupied or to be occupied by the borrower.

B. To clarify the existing authority of Federal associations to exercise due on sale clauses, and limit the circumstances under which such clauses can be exercised on future loans on the security of a home occupied or to be occupied by the borrower.

LATE CHARGES

[Omitted]

DUE ON SALE

It is the position of the Board that "due on sale" clauses are authorized for Federal associations under §545.6-11, the Board regulation governing the terms of the loan documents used by Federal associations.

While there are may [sic] variants of the "due on sale" clause in common use in security transactions in real property, they typically provide for the acceleration of the maturity of the loan — at the option of the lender — upon the sale or transfer by the borrower of all or any part of the real property securing the loan, unless the lender has given its prior consent to such sale or transfer.

There are three commonly assigned reasons underlying the exercise of "due on sale" clauses. Such clauses enable the lending savings and loan association to —

(1) Ensure that the real property securing its loan is not sold, subject to its loan, to a person of doubtful financial stability, and to assure that its loan is not assumed by a new purchaser whom the association does not consider to be creditworthy;

(2) Adjust its loan portfolio towards current market rates, thus safeguarding and protecting the financial stability of the association and permitting it to make new home loans at lower interest rates than otherwise would be necessary to maintain an adequate yield on its mortgage portfolio; and

(3) Sell its existing home loans in the secondary mortgage market in an orderly manner, thereby generating substantial new funds for additional residential loans, which otherwise would be unavailable.

The Board believes that a contractual ability to repay the loan and property [sic] exercisable by a Federal association for any of the foregoing reasons. The Board is of the view that the financial security and stability of Federal associations would be endangered if the loan is, as a practical matter, assumed by a new borrower without credit underwriting by the association in connection with the sale of the security property. If the security property is transferred to a person whose ability to repay the loan and properly maintain the property is inadequate, the Board believes that the lending association's ability to protect its vital security interest is endangered. The Board also is of the view that elimination of the due on sale clause will cause a substantial reduction of the cash flow and net income of Federal associations, and that to offset such losses it is likely that the associations will be forced to charge higher interest rates and loan charges on home loans generally. The Board is concerned that such higher rates and/or charges could adversely affect home buyers generally, and particularly younger families who are purchasing their first home — the

group which ordinarily can least afford the additional expenses. The Board further is of the view that elimination of the due on sale clause will restrict and impair the ability of Federal associations to sell their home loans in the secondary mortgage market, by making such loans unsalable or causing them to be sold at reduced prices, thereby reducing the flow of new funds for residential loans, which otherwise would be available. Any such reduction would adversely affect home buyers, the house industry and the national economy. Lastly, the Board is of the view that elimination of the due on sale clause will benefit only a limited number of home sellers, but generally will cause economic hardship to the majority of home buyers and potential home buyers.

The Board notes that the majority of courts which considered the matter have upheld the validity of due on sale clauses used by savings and loan associations. However, recently the authority of Federal associations to exercise their contractual due on sale clauses has been the subject of controversy and litigation in certain States. Therefore, the Board deems it desirable to amend §545.6-11 to clarify the existing authority of Federal associations to include due on sale clauses in their loan contracts with borrowers and to exercise such clauses. The Board also deems it desirable to include in such amendment limitations on the exercise by Federal associations of their existing due on sale authority as to certain future loans.

Paragraph (f) of the proposed amendment would provide that a Federal association continues to have the power to include, solely as a matter of contract between it and its borrowers, provisions in its loan contracts and/or loan instruments whereby the association may, at its option, declare the entire amount of the loan is immediately due and payable if all or any part of the real property securing the loan is

sold or transferred by the borrower without the association's prior written consent. Paragraph (f) would provide further that, except as provided in paragraph (g) with respect to loans made after May 31, 1976, on the security of a home occupied or to be occupied by the borrower, the exercise by a Federal association of any option to accelerate the maturity of its existing or future loans in the event of a sale or transfer by the borrower of all or any part of the loan security property without the prior written consent of the association shall be exclusively governed by the terms of the loan contract between such association and the borrower, and that all rights and remedies of the association and borrower respecting such acceleration shall be fixed and governed by said loan contract. The provisions of paragraph (f) would apply to any sale or transfer of the loan security property by the borrower, except for the specific transactions delineated in paragraph (g), including any sale or transfer through an installment, land contract or similar means of sale.

Paragraph (g) of the proposed amendment would provide three limitations on a Federal association's contractual right to exercise due on sale clauses as to loans made after May 31, 1976, on the security of a home occupied or to be occupied by the borrowers. First, a Federal association's contractual option to accelerate the maturity of the loan in the event of a sale or transfer by the borrower of all or any part of the loan security property without the prior written consent of the association would not apply to, and would exclude, the following transactions respecting the loan security property: (i) the creation of a lien or encumbrance subordinate to the association's mortgage or deed of trust; (ii) the creation of a purchase money security interest for household appliances; (iii) a transfer by devise, descent or by operation of law upon the death of a joint tenant; or (iv)

the grant of any leasehold interest of three years or less not containing an option to purchase.

Second, a Federal association would waive any contractual option to accelerate if, prior to the sale or transfer of the loan security property, the association and the person to whom the property is to be sold or transferred reach agreement in writing that the credit of such person is satisfactory to the association and that the interest payable to the association on sums secured by its note, mortgage and/or deed of trust shall be at such rate as the association shall request. The Board anticipates that the association will request a rate consistent with the then prevailing rate charged by the association on loans of similar amount and maturity with respect to similar types of security property to borrowers of similar credit-worthiness. Further, if the Federal association has waived its option to accelerate as provided in paragraph (g), and if the borrower's successor in interest has executed a written assumption agreement of the loan accepted in writing by the association, the association would release the borrower from all obligations under the note, mortgage and/or deed of trust securing the loan, and solely for the purpose of §541.14(a) of the Federal Regulations the association would be deemed to have made a new loan to the borrower's successor in interest.

The foregoing limitations on the exercise of due on sale clauses closely parallel the provisions contained in the standard loan documents used jointly by the Federal Home Mortgage Corporation and the Federal National Mortgage Association. Thus, many Federal savings and loan associations throughout the Nation already are following such limitations on the exercise of due on sale clauses in connection with billions of dollars in residential home loans which they originated and sold — in whole or in part — to the Federal Home Loan Mortgage Corporation or to the

Federal National Mortgage Association and to the Government National Mortgage Association.

Third, a Federal association would be precluded from imposing a prepayment penalty, or equivalent charge, on the borrower upon the acceleration of the maturity of the loan, and the payment thereof by the borrower, due to the exercise by the association of its contractual due on sale clause.

Aside from the three limitations set forth above, Federal associations may elect, as they have done in the past in individual cases, to waive their contractual due on sale rights when, in their judgment, unusual hardships exist respecting particular borrowers.

Interested persons are invited to submit written data, views and arguments to the Office of the Secretary, Federal Home Loan Bank Board, 320 First Street, N.W., Washington, D.C. 20552, by March 22, 1976, as to whether this proposal should be adopted, rejected, or modified. Written material submitted will be available for public inspection at the above address.

The Federal Home Loan Bank Board considers it desirable to amend Part 545 of the rules and regulations for the Federal Savings and Loan System (12 CFR Part 545), for the purposes described below. Accordingly, the Board hereby purposes to amend said Part 545 by adding new paragraphs (d), (e), (f) and (g) to §545.6-11, to read as set forth below.

§545.6-11 LOAN CONTRACT.

(d) [Omitted]

(e) [Omitted]

(f) *Due on sale clauses.* A Federal association continues to have the power to include, as a matter of contract between it and the borrower, a provision in its loan contract

and/or loan instruments whereby the Federal association may, at its option, declare the entire amount of the loan immediately due and payable if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent. Except as provided in paragraph (g) of this section with respect to loans made after May 31, 1976, on the security of a home occupied or to be occupied by the borrower, the exercise by a Federal association of any option to accelerate the maturity of existing or future loans in the event of a sale or transfer by the borrower of all or any part of the loan security property without the prior written consent of the association shall be governed exclusively by the terms of the loan contract between the association and the borrower, and all rights and remedies of the association and borrower respecting such acceleration shall be fixed and governed by said loan contract.

(g) *Limitations on the exercise of due on sale clauses.* (1) With respect to any loan made after May 31, 1976, on the security of a home (as defined by §541.10-2) occupied or to be occupied by the borrower, a Federal association's contractual option to accelerate the maturity of the loan in the event of a sale or transfer by the borrower of all or any party of the loan security property without the prior written consent of the association shall not apply to, and shall exclude, the following transactions respecting the loan security property:

(i) The creation of a lien or encumbrance subordinate to the association's mortgage or deed of trust;

(ii) The creation of a purchase money security interest for household appliances;

(iii) A transfer by devise, descent or by operation of law upon the death of a joint tenant; or

(iv) The grant of any leasehold interest of three years or less not containing an option to purchase.

(2) Further, with respect to any aforesaid loan made after May 31, 1976, no Federal association shall impose a prepayment penalty, or equivalent charge, on the borrower upon the acceleration of the maturity of the loan, and the payment thereof by the borrower, due to the exercise by the association of its contractual option to accelerate as a result of the sale or transfer by such borrower of all or any part of the loan security property without the written consent of the association. With respect to loans governed by this paragraph, a Federal association shall have waived any contractual option to accelerate if, prior to the sale or transfer of the loan security property, the association and the person to whom the property is to be sold or transferred reach agreement in writing that the credit of such person is satisfactory to the association and that the interest payable to the association on sums secured by its note, mortgage and/or deed of trust shall be at such rate as the association shall request. If the Federal association has waived its option to accelerate as provided in this paragraph, and if the borrower's successor in interest has executed a written assumption agreement of the loan accepted in writing by the association, the association shall release the borrower from all obligations under the note, mortgage and/or deed of trust securing the loan, and solely for the purpose of §541.14(a) the association shall be deemed to have made a new loan to the borrower's successor in interest.

(Sec. 5, 48 Stat. 132, as amended; 12 U.S.C. §1464, Reorg. Plan No. 3 of 1947, 12 FR 4981, 3 CFR, 1943-48 Comp., p. 1071)

By the Federal Home Loan Bank Board.

[SEAL]

J.J. Finn,
Secretary.

Federal Home Loan Bank Board Resolution No. 76-296

[41 Fed. Reg. 18,286 (1976)]

[in pertinent part]

Amendments Relating to Late Charges and Due-on-Sale Clauses

Summary. The following summary of the amendments adopted by this Resolution is provided for the reader's convenience and is subject to the full explanation in the following preamble and to the specific provisions of the amendments.

I. *Present Situation.* The Federal Home Loan Bank Board permits Federal associations, if authorized by their loan contracts, to assess, impose, and collect late charges respecting delinquent periodic installment payments on such loans, and to declare the loan immediately due and payable if the borrower sells or transfers the real property securing the loan without the consent of the association.

II. *Final Amendment.* A. A Federal association continues to be empowered to include, as a matter of contract between it and the borrower, provisions in its loan contracts for assessment, imposition, and collection of a late charge respecting any delinquent periodic installment payment, and for the acceleration of the maturity of the loan, at the option of the association, if the borrower sells or transfers the loan security property without prior written consent of the association.

B. Limits are placed on the imposition and maximum amount of late charges which may be collected by a Federal association on future loans secured by borrower-occupied homes.

C. Restrictions are placed on exercise of acceleration (due-on-sale) clauses contained in future loan contracts secured by borrower-occupied homes.

III. *Differences from Proposal.* A. Late charges 1. A late charge may be imposed if an installment payment is not received by the association within the grace period; proposal used date-of-payment concept including payment by deposit in the mail.

2. The alternative seven-day delinquency notice requirement in proposal is deleted; associations are required to make disclosure of late-charge provisions in any monthly billings.

3. A new Statement of Policy is issued regarding disclosure and imposition of late charges in connection with existing loans.

B. *Due-on-sale Clauses.* A new Statement of Policy is issued regarding exercise of due-on-sale clauses and loan assumptions.

C. *Effective Date.* Effective date is 7/31/76; proposal specified 5/31/76.

By Resolution No. 76-100 of February 6, 1976, the Federal Home Loan Bank Board proposed to amend §545.6-11 of the Rules and Regulations for the Federal Savings and Loan System (12 CFR 545.6-11) for the purposes of clarifying and limiting the authority of Federal savings and loan associations in the area of late charges and due-on-sale clauses. Notice of such proposed rulemaking was duly published in the FEDERAL REGISTER on February 12, 1976 (41 FR 6283-6287), with an invitation for interested persons to submit comments by March 22, 1976. On the basis of all relevant material presented by interested persons and otherwise available, the Board hereby adopts the changes as proposed, with modifications discussed below.

* * *

Paragraphs (f) and (g) of §545.6-11, relating to Federal associations' authority regarding due-on-sale clauses, are

adopted substantially as proposed, with some portions rewritten or re-numbered for clarification purposes only. The effective date of the limitations is July 31, 1976.

A new Statement of Policy clarifying and interpreting the Board's policies pertaining to late charges and due-on-sale clauses is adopted by the Board at §556.9. Paragraph (a) expresses the Board's view that all contract terms affecting the borrower should be fully disclosed no later than the time of loan closing. Paragraph (b)(1) states that the Board disfavors the practice of imposing prepayment charges upon exercise of due-on-sale clauses with regard to loans made prior to August 1, 1976, on the security of borrower-occupied homes, and urges associations to curtail this practice in connection with such earlier loans in the absence of extraordinary circumstances. Paragraph (b)(2) describes considerations relevant to imposition of late charges with regard to loans made prior to August 1, 1976. Paragraph (c) expresses the Board's view that there may be circumstances other than those described in §545.6-1(g)(1) where an association should consider waiver of its acceleration option. Paragraph (d) states the Board's expectation that, in transactions covered by the loan assumption provision of §545.6-11(g)(3), associations should not increase interest rates to rates in excess of current-market interest rates for comparable loans made by the associations applying their normal underwriting standards. New paragraph (e) states the Board's interpretation with respect to maintenance of mortgage insurance in connection with the requirements of paragraph 545.6-11(g)(3).

Finally, it was and is the Board's intent to have late charges and due-on-sale practices of Federal associations governed exclusively by Federal law. Therefore, charging of late charges and exercise of due-on-sale clauses by Federal associations shall be governed and controlled solely by

§545.6-11 and the Board's new Statement of Policy. Federal associations shall not be bound by or subject to any conflicting State law which imposes different late charges or due-on-sale requirements, nor shall Federal associations attempt to impose a higher late charge than permitted in §545.6-11(e) or avoid the limitations on the exercise of due-on-sale clauses delineated in §545.6-11(g) on the ground that such higher charge or avoidance of limitations is permissible under State law.

Accordingly, the Board hereby revises §545.6-11 and adds §556.9 to read as set forth below, effective June 8, 1976.

1. Section 545.6-11(d) is revised to read as set forth below.

§545.6-11 LOAN CONTRACT

* * *

(f) *Due-on-sale clauses.* A federal association continues to have the power to include, as a matter of contract between it and the borrower, a provision in its loan instruments whereby the association may, at its option, declare immediately due and payable all of the sums secured by the association's security instrument if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent. Except as provided in paragraph (g) of this section with respect to loans made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, exercise by an association of such an acceleration option (hereafter called a due-on-sale clause) shall be governed exclusively by the terms of the contract between the association and the borrower, and all rights and remedies of the association and borrower thereto shall be fixed and governed by said contract.

(g) *Limitations on the exercise of due-on-sale clauses.* (1) With respect to any loan made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, a Federal association may not exercise a due-on-sale clause based on any of the following:

(i) creation of a lien or other encumbrance subordinate to the association's security instrument;

(ii) creation of a purchase money security interest for household appliances;

(iii) transfer by devise, descent, or by operation of law upon th death of a joint tenant; or

(iv) grant of any leasehold interest of three years or less not containing an option to purchase.

(2) With respect to any loan made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, no Federal association shall impose a prepayment charge or equivalent fee in connection with the acceleration of the loan pursuant to the exercise of a due-on-sale clause.

(3) With respect to any loan made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, a Federal association shall have waived its option to exercise a due-on-sale clause as to a specific transfer if, prior to that transfer, the association and the person to whom the property is to be sold or transferred (the existing borrower's successor in interest) reach written agreement that the credit of such person is satisfactory to the association and that the interest payable to the association on sums secured by its security instrument shall be at such rate as the association shall request. Upon such written agreement and resultant waiver, the association shall release such existing borrower from all obligations under the loan instruments, and for purposes of §541.14(a) the association shall

be deemed to have made a new loan to such existing borrower's successor in interest.

2. Section 556.9 is added to read as set forth below:

§556.9 IMPOSITION OF LATE CHARGES AND DUE-ON-SALE CLAUSES.

(a) The Board allows Federal savings and loan associations certain authority to incorporate into loan instruments provisions for imposition of late charges, prepayment charges, and exercise of acceleration clauses, including due-on-sale clauses. The Board expects associations to adopt procedures sufficient to ensure that, no later than the time of loan closing, the rights and obligations of the contracting parties under these provisions are fully and specifically disclosed to borrowers.

(b)(1) Imposition of a prepayment charge upon exercise of a due-on-sale clause is prohibited pursuant to §545.6-11 (g)(2) of this subchapter only with regard to loans made upon borrower-occupied homes after July 31, 1976; however, the Board looks with disfavor upon such practice respecting all loans made on the security of borrower-occupied homes, and believes that associations should abstain therefrom in connection with such loans made before such date, except in extraordinary circumstances.

(2) Although there is no maximum limitation on the amount of late charges which a Federal association may assess or collect, pursuant to contract, on loans made prior to August 1, 1976, on the security of borrower-occupied homes, the Board expects associations to continue to be reasonable and fair in assessing, imposing, and collecting late charges against delinquent borrowers as to such loans, taking into consideration the reason for the delinquency, and the past practice of the borrower respecting delinquencies.

(c) Paragraph 545.6-11(g)(1) of this subchapter prohibits with respect to borrower-occupied-home loans made after July 31, 1976, exercise of due-on-sale clauses to accelerate the loan based on creation of junior liens, certain purchase-money security interests, transfers by devise, descent, or by operation of law upon the death of a joint tenant, and certain short-term leasehold interests. However, the Board believes that there may be other situations respecting loans made on the security of borrower-occupied homes in which, depending on the circumstances of the individual case, it will be appropriate for Federal associations to waive their contractual right to accelerate. These situations include transfers of title to members of the borrower's immediate family, including a former spouse in connection with a divorce, who occupy or will occupy the property (to the extent not covered by paragraph 545.6-11(g)(1)(iii)). In addition, associations should consider waiving any right to require an increase in interest rate pursuant to a due-on-sale clause in cases of extreme hardship to the existing borrower.

(d) Paragraph 545.6-11(g)(3) of this subchapter authorizes Federal associations to increase the interest rate as a condition of loan assumption. However, the Board expects that no association will request an increase in the interest rate to a rate in excess of the then prevailing rate on comparable new loans made by the association applying its normal underwriting standards.

(e) The Board does not interpret paragraph 545.6-11(g)(3) of this subchapter to preclude an association from requiring, as a condition to an assumption, the continued maintenance of mortgage insurance by the existing borrower's successor in interest, whether by endorsement of a policy previously procured by the existing borrower or by entrance into a new contract of insurance.

(Sec. 5, 48 Stat. 132, as amended; 12 U.S.C. §1464. Reorg. Plan No. 3 of 1947, 12 F.R. 4981, 3 CFR, 1943-48 Comp., p. 1071)

By the Federal Home Loan Bank Board.

[SEAL]

J. J. FINN,
Secretary.

12 C.F.R. §545.8-3(f) and (g) (1981)*

"(f) *Due-on-sale clauses.* An association continues to have the power to include, as a matter of contract between it and the borrower, a provision in its loan instrument whereby the association may, at its option, declare immediately due and payable sums secured by the association's security instrument if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent. Except as provided in paragraph (g) of this section with respect to loans made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, exercise by the association of such option (hereafter called a due-on-sale clause) shall be exclusively governed by the terms of the loan contract, and all rights and remedies of the association and borrower shall be fixed and governed by that contract."

"(g) *Limitations on the exercise of due-on-sale clauses.* With respect to any loan made after July 31, 1976, on the security of a home occupied or to be occupied by the borrower, a Federal association: (1) Shall not exercise a due-on-sale clause because of (i) creation of a lien or other encumbrance subordinate to the association's security instrument, (ii) creation of a purchase money security interest for household appliances; (iii) transfer by devise, descent, or operation of law on the death of a joint tenant; or (iv) granting of a leasehold interest of three years or less not containing an option to purchase; (2) shall not impose a prepayment charge or equivalent fee for acceleration of the loan by exercise of a due-on-sale clause; and

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*The Federal Home Loan Bank Board's "due-on-sale" regulation, originally promulgated as 12 C.F.R. §545.6-11(f) and (g), was renumbered as 12 C.F.R. 545.8-3(f) and (g) in 1979. See 44 Fed. Reg. 39,108 (1979) and 44 Fed. Reg. 7,386 (1979).

(3) waives its option to exercise a due-on-sale clause as to a specific transfer if, before the transfer, the association and the person to whom the property is to be sold or transferred (the existing borrower's successor in interest) agree in writing that the person's credit is satisfactory to the association and that interest on sums secured by the association's security interest will be payable at a rate the association shall rquest. Upon such agreement and resultant waiver the association shall release the existing borrower from all obligations under the loan instruments, and the association is deemed to have made a new loan to the existing borrower's successor in interest."

Federal Home Loan Bank Board Resolution No. 81-409

[46 Fed. Reg. 39,123 (1981)]

STATEMENT OF POLICY REGARDING DUE-ON-SALE CLAUSES IN MORTGAGE LOAN CONTRACTS

July 23, 1981.

AGENCY: Federal Home Loan Bank Board.

ACTION: Final rule.

SUMMARY: The Board is reiterating its longstanding policy regarding the preemptive nature of its regulations authorizing Federally-chartered savings and loan associations to include due-on-sale clauses in their mortgage loan contracts and to exercise such clauses subject only to express limitations imposed by the Board. The Board is taking this action in order to allay the uncertainty expressed by a few State Courts.

EFFECTIVE DATE: July 23, 1981.

FOR FURTHER INFORMATION CONTACT: Harvey Simon, Associate General Counsel, Office of General Counsel, Federal Home Loan Bank Board, 1700 G Street, N.W., Washington, D.C. 20552, (202-377-6420).

SUPPLEMENTARY INFORMATION: On July 31, 1976, the Federal Home Loan Bank Board codified its Confirmation of the authority of Federal savings and loan associations to include and exercise acceleration or "due-on-sale" clauses in their mortgage loan contracts subject only to such limitations as the Board imposed. In Board Resolution No. 76-296, 41 FR 18286 (May 3, 1976), the Board added new due-on-sale provisions to its regulation pertaining to loan contracts (12 CFR 545.6-11) and to its statements of policy (12 CFR 556.9).

New paragraph (f) of Federal Regulation §545.6-11, now re-codified at §545.8-3(f), provided:

A Federal association continues to have the power to include, as a matter of contract between it and the borrower, a provision in its loan instruments whereby the association may, at its option, declare immediately due and payable sums secured by the association's security instrument if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent * * *.

In addition, in the preamble contained in Resolution No. 76-296, the Board stated:

[I]t was and is the Board's intent to have * * * due-on-sale practices of Federal associations governed exclusively by Federal law. Therefore, * * * exercise of due-on-sale clauses by Federal associations shall be governed and controlled solely by §545.6-11 and the Board's new Statement of Policy. Federal associations shall not be bound by or subject to any conflicting State law which imposes different * * * due-on-sale requirements * * *.

Notwithstanding these plain pronouncements, the Board now considers it desirable to re-affirm explicitly the preemptive nature of its due-on-sale regulations by codification in the policy statement at 12 CFR 556.9, in order to allay the uncertainty expressed by a few state courts regarding this matter. The Board also has taken this opportunity to set forth its judgment regarding the importance of due-on-sale clauses to Federal associations, and to codify its rationale for authorizing rather than compelling use of the due-on-sale clause by Federal associations, i.e. to provide greater flexibility to associations in tailoring their mortgage documents to accommodate special circumstances.

The Board finds that observance of the notice and public comment procedures and delay of effective date required pursuant to §§508.12 and 508.14, and 5 U.S.C. 553(b) and

(d), respectively, would be unnecessary because this amendment pertains to a general statement of policy.

Accordingly, the Board hereby amends Part 556 of Subchapter C, Chapter V, Title 12 of the Code of Federal Regulations, as set forth below.

SUBCHAPTER C — FEDERAL SAVINGS AND LOAN SYSTEM

PART 556 — STATEMENTS OF POLICY

Amend §556.9 by adding a new paragraph (f) thereto, to read as follows:

§556.9 IMPOSITION OF LATE CHARGES AND DUE-ON-SALE CLAUSES.

* * *

(f) *Due-on-sale Policy and Federal preemption.* (1) Federal associations are obliged to take reasonable precautions to protect themselves against the economic risks associated with mortgage lending, including the risk that the cost of lendable funds will exceed the yield from existing mortgage loans, and that sharply rising interest rates will reduce substantially the value of existing mortgage assets. In this connection, the Board has determined that the due-on-sale clause normally is a valuable and often an indispensable source of protection for the financial soundness of Federal associations and for their continued ability to fund new home loan commitments. Consequently, the Board for many years has authorized due-on-sale clauses for use by Federal associations. However, because the Board desires to afford associations the flexibility to accommodate special situations and circumstances, §545.8-3(f) of this Subchapter by its terms merely authorizes rather than compels the inclusion and exercise of due-on-sale clauses in mortgage loans.

(2) Paragraph (f) of §545.8-3 confirms the continuing authority of Federal associations to include due-on-sale clauses in their mortgage loan contracts and to exercise such clauses, subject only to the express limitations contained in §545.8-3(g). Due-on-sale practices of Federal associations shall be governed exclusively by the Board's regulations, in preemption of and without regard to any limitations imposed by state law on either their inclusion or exercise (including, but not confined to, state law prohibitions against restraints on alienation, prohibitions against penalties and forfeitures, equitable restrictions and state law dealing with equitable transfers).

(Sec. 5, 48 Stat. 132, as amended; (12 U.S.C. 1464), Reorg. Plan No. 3 of 1947; 3 CFR, 1943-48 Comp.)

By the Federal Home Loan Bank Board.

J. J. Finn,
Secretary.

California Civil Code §711

"Conditions restraining alienation, when repugnant to the interest created, are void." (Cal. Civ. Code §711 (West 1954).)

Motion to Dismiss or Affirm

Office - Supreme Court, U.S.
FILED
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No.81-1139

SUPREME COURT
of the
UNITED STATES
October Term, 1981

Glendale Federal Savings and Loan Association and
Verdugo Service Corporation,

Appellants,

vs.

Dean L. Gross and Pedro Enriquez,

Appellees.

On Appeal from the Court of Appeal
State of California
Fourth Appellate District, Division Two.

MOTION TO DISMISS OR AFFIRM

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QUESTIONS PRESENTED

1. Is there a true preemption issue before the Court? Subissues include:

a. Does *Wellenkamp* constitute "state law" of a type subject to federal preemption?

b. Does the subject federal regulation promote nationwide uniformity?

c. Does the state court decision find support in the constitution notwithstanding appellants' narrow focus on the subject federal regulation?

d. Is the subject federal regulation wholly incompatible with *Wellenkamp?*

2. Would the Court of Appeal of California have reached the same result applying universally accepted principles of contract law, pursuant to the mandate of the subject federal regulation?

MOTION TO DISMISS OR AFFIRM

Appellees (sometimes referred to herein as "plaintiffs"), pursuant to Rule 16 of the Revised Rules of the Supreme Court of the United States, respectfully move this Honorable Court to dismiss the above entitled appeal or, in the alternative, to affirm the judgment of the Court of Appeal of California on the following grounds:

1. The federal question of preemption raised by appellants (sometimes referred to herein as "defendants") is illusory [Rule 16 (d)];

2. The same result would have obtained had the state court applied the subject federal regulation in this case. [Rule 16 (d)].

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No. 81-1139

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October Term, 1981

Glendale Federal Savings and Loan Association and Verdugo Service Corporation,

Appellants,

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Dean L. Gross and Pedro Enriquez,

Appellees.

On Appeal from the Court of Appeal

State of California

Fourth Appellate District, Division Two.

MOTION TO DISMISS OR AFFIRM

I

STATEMENT

The federal question presented in Appellants' Jurisdictional Statement is framed as one of federal preemption.[1] Appellants argue that 12 C.F.R. § 545.8-3 (f) and (g) (the "subject federal regulation"), promulgated by the Federal Home Loan Bank Board ("FHLBB") pursuant to the Home Owners' Loan Act of 1933, 12 U.S.C. § 1464 *et seq.* ("HOLA"), which allows a federal association to "continue to have the power to include, as a matter of contract

1. Jurisdictional Statement, p. i.

between it and the borrower," a due-on-sale clause in its loan instrument, conflicts with and preempts California Civil Code § 711, prohibiting conditions restraining alienation, as interpreted by the California Supreme Court in *Wellenkamp v. Bank of America* 21 Cal. 3d 943, 582 P. 2d 970, 148 Cal. Rptr. 379 (1978).

Appellees, in this motion, contend that preemption is an illusory issue; that the *Wellenkamp* decision does not fit into the classic mold of "state law" to which the preemption doctrine is applied; that the constitutional considerations in this case are broader than merely the question of preemption and tend to support the state court ruling; and that the federal law invoked by appellants mandates the application of principles of contract law, under which the state court would have reached the same decision.

Wellenkamp held that automatic exercise of a due-on-sale clause is an unlawful restraint on alienation.

Appellants contend, in substance, that the *Wellenkamp* precedent constitutes "state law" as the term is used in the context of the doctrine of federal preemption; that the subject federal regulation constitutes "federal law"; that the two laws are in direct and unavoidable conflict; that the federal law therefore preempts the state law; and that the federal law permits the automatic exercise of the due-on-sale clause under the circumstances in this case.

II

ARGUMENT

A. DEFENDANTS' PREEMPTION ARGUMENT IS ILLUSORY, AND IS BASED ON A SERIES OF FALSE ASSUMPTIONS.

1. FALSE ASSUMPTION NO. 1: *WELLENKAMP* CONSTITUTES " STATE LAW" AS THAT TERM IS USED IN CLASSIC PREEMPTION CASES.

A sampling of preemption cases demonstrates that the doctrine of preemption applies where a state *law* or *legislative* scheme conflicts with a federal law or legislative scheme. See, *e.g., Gibbons v. Ogden,* 22 U.S. (9 Wheat.) 1 (1824) [New York navigation rights]; *Huron Portland Cement Co. v. Detroit, 362 U.S. 440 (1960) [Detroit Smoke Abatement Code]; Ray v. Atlantic Richfield Co.,* 435 U.S. 151 (1978) [Washington Tanker Law]; *Parker v. Brown,* 317 U.S. 341 (1942) [California Agricultural Prorate Act]; *Meyers v. Beverly Hills Federal Savings and Loan Association,* 499 F. 2d 1145 (9th Cir. 1974) [California liquidated damages laws]; *Rice v. Santa Fe Elevator Corp,* 311 U.S. 218 (1947) [Illinois Warehouseman laws]; *City of Burbank v. Lockheed Air Terminal, Inc.,* 411 U.S. 624 (1973) [Municipal noise ordinance]; *Florida Lime and Avocado Growers, Inc. v. Paul,* 373 U.S. 132 (1963) [§792 of the California Agricultural Code].

While the *Wellenkamp* decision was based on California Civil Code § 711, that code section merely incorporates into the state system of codification the common law rule against restraints on alienation (*Wharton v. Mollinet*, 103 Cal. App. 2d 710, 713 [1951]), so that the *Wellenkamp* decision was not dependent upon Civil Code §711 or any other state enacted legislation (see, *Churchill v. Pacific Impr. Co.*, 96 Cal. 490, 493 [1892]). Consequently, *Wellenkamp* does not merely speak to a parochial legislative act endemic only to the State of California, but it speaks a basic tenet of the common law. That decision is not analogous to the "state law" addressed in preemption cases.

Since the common law tenet to which *Wellenkamp* speaks involves the constitutionally-protected right to own, use and dispose of property (see *Terrace v. Thompson*, 263 U.S. 197, 215 [1923]), which should be construed to include the common law rule against restraints on alienation (cf. *Ex parte Grossman*, 267 U.S. 87, 108-9 [1924]); and since it is within the province of a state court to construe a constitutionally-protected right (see, generally, *Parker v. Brown, supra*, referencing *Agricultural Prorate Commission v. Superior Court*, 5 Cal. 2d 550; *State ex rel. Ricco v. Biggs*, 198 Or. 413, 225 Pac. 2d 1055, 1063 [1953]; *Miller v. Municipal Court*, 22 Cal. 2d 818, 827 [1943], citing *Marbury v. Madison*, 5 U.S. [1 Cranch] 137

[1803]), the *Wellenkamp* decision speaks with authority that transcends a state law subject to the doctrine of federal preemption. Indeed, a court decision construing a constitutionally-protected common law right (*Terrace v. Thompson, supra)* warrants consideration even outside its own jurisdiction, based on principles of due process (cf. *Pae v. Stevens,* 256 F. 2d 208, 215 [9th Cir. 1958]) and should not wilt in the fact of a federal regulation which, affecting that right, may not enjoy a presumption of constitutional validity (see *Ex parte Mitsuye Endo,* 323 U.S. 283, 295 [1944]; *Cash v. Hoch,* 309 F. Supp. 347, 348 [W.D. Wis. 1970]; *Patterson v. Daquet,* 62 Misc. 2d 106, 308 N.Y.S. 2d 173 180-1 [1969]; *Ex parte Rhodes,* 79 So. 462, 1 A.L.R. 568). In effect, *Wellenkamp,* itself, echoes with a ring of constitutional authority and should not be summarily swept under the carpet of preemption.

2. FALSE ASSUMPTION NO. 2: PREEMPTION IS NECESSARY IN THIS MATTER TO ESTABLISH UNIFORMITY IN THE LENDING PRACTICES OF FEDERALLY CHARTERED ASSOCIATIONS.

The keystone of the doctrine of preemption, that federally regulated activities should not become bogged down by diverse local regulations, has been employed to support the preemption argument with respect to the subject federal regulation. See *Glendale Federal Savings and Loan Association v. Fox,* 459F. Supp. 903, 908 (C.D. Cal. 1978).

The *Fox* rationale dissembles the facts. Not only does the subject regulation fail to promote nationwide uniformity, but it creates a dangerous lack of uniformity *within* the state.

The language of the subject regulation allows each individual lender the option of including the due-on-sale clause in its loan instruments, and additionally allows each lender the further option of enforcing the clause. It also allows that individual borrowers may bargain against inclusion of the clause, so that any given lender might not uniformly use the due-on-sale clause from borrower to borrower. Consequently, there is nothing in the language of the regulation which evidences an intent to promote nationwide uniformity.

Although, in practice, it appears that the due-on-sale clause is uniformly employed by federal lenders and that individual borrowers have no bargaining strength to exclude the clause, this also leads to a lack of nationwide uniformity. Evidence can be produced that would show that the average per capita income of a California resident is approximately fifteen percent (15%) higher than the national average[2], but that the average price of a home in California is approximately one hundred twenty percent (120%) higher than the national average![3] It can be

2. Source: Bureau of Economic Analysis, U.S. Commerce Department

3. Source: Department of Housing and Urban Development

inferred that the burden imposed by the due-on-sale clause is not uniformly borne from state to state, and where in one locale it may have some salutary effect, in others, like California where a difference of even one percentage point in a home loan represents a substantial drain on the borrower's monthly budget, the presence of a due-on-sale clause in federal loans has produced a myriad of deleterious side effects, including the emergence of a federal-loan-assumption "black market", which makes a mockery of the deed recording system and involves six-digit-figure transactions based on makeshift, untested instruments, some of which are drafted by real estate agents and not even reviewed by licensed attorneys. It would appear that the due-on-sale clause does nothing to promote nationwide uniformity either in theory or in practice.

Since federal lending institutions are confined to the territorial boundaries of their respective states, the premium should not be on nationwide uniformity, but on statewide uniformity. In California, only federal lenders now automatically enforce due-on-sale clauses. This causes a tremendous disparity in rights between a borrower with a federal lender and one who had fortuitously borrowed from a state lender. It is a cruel irony, in light of the original purposes of HOLA, that it is the former who now feels that he or she is being thrown to the financial wolves.

3. FALSE ASSUMPTION NO. 3: THE ONLY CONSTITUTIONAL PRINCIPLES BEARING ON THIS MATTER ARE THE SUPREMACY CLAUSE AND THE DOCTRINE OF FREEDOM OF CONTRACT.

Inherent in defendants' grossly oversimplified characterization of the issue in this and related cases as simply one of preemption is the assumption that the only constitutional principles applicable are the supremacy clause as relating to federal legislation and the doctrine of freedom of contract. Defendants self-righteously mantle their arguments with these lofty sounding maxims and disdainfully reproach plaintiffs' attempt to exercise plebian state-developed rights in derogation of these majestic constitutional precepts ostensibly favoring defendants. Although this Court does not have to reach the question of preemption or any other constitutional questions in resolving this case, see section II, B, *infra*, it should nevertheless be pointed out that defendants, under the erroneous assumption that their actions are sanctioned by the subject federal regulation, are themselves running roughshod over the very constitution they sanctimoniously invoke.

For example, as discussed under subsection II, A, 1, *supra*, the *Wellenkamp* decision would lend strong support to an argument that unbridled exercise of the due-on-sale clause unjustifiably infringes on the constitutionally-protected substantive right to own property. See *Terrace v. Thompson*, *supra*.

Also, as discussed under subsection II, A, 2, *supra*, the invocation of the subject federal regulation in the state courts to justify the unrestrained use of the due-on-sale clause creates an unequal hardship on certain California buyers saddled with federal loans (the distinction between state and federal lenders is generally lost on borrowers) arguably denying them equal protection under the law. Cf. *Shelley v. Kraemer*, 334 U.S. 1 (1974) [The Constitution confers upon no individual the right to demand action by the State which results in the denial of equal protection of the laws to other individuals.]; *Sie Fujii v. State of California*, 38 Cal.2d 718 (1952) [Restrictions on land ownership which arbitrarily discriminate against a particular catagory of residents violate the Fourteenth Amendment.].

Thirdly, as discussed under subsection II, A, 2, *supra*, and under section II, B, *infra*, the federal lender purportedly has federally-sanctioned power to arbitrarily withhold or include a due-on-sale clause in any given loan instrument and to arbitrarily enforce such a clause at its discretion, where the borrower has no real choice in the matter. If indeed, such a power were to exist unchecked by external forces offering reasonable protections to the borrower, it would appear to run afoul of fundamental tenets of due process. See Adams v. Egley, 338 F. Supp. 614 (S.D. Cal. 1972) [Summary repossession of property

by private party without notice and hearing constitutes a wrongful taking.] See also *Fuentes v. Shevin*, 407 U.S. 67 (1971). Further, it would deny the borrower, who in today's commercial climate must often look to the state for bargaining leverage to obtain reasonable terms in contracts with the monolithic cabal of overreaching lending institutions, *his or her* constitutional right to freely contract.[4]

There may be other constitutional issues applicable to this case, but the matter does not require a resolution on constitutional grounds and the preceding examples should suffice to illustrate the invalidity of defendants' claim of an unassailable constitutional position.

4. FALSE ASSUMPTION NO. 4: THE SUBJECT FEDERAL REGULATION ALLOWS FEDERAL LENDERS THE ABSOLUTE RIGHT TO AUTOMATICALLY ENFORCE THE DUE-ON-SALE CLAUSE.

The language of the subject federal regulation expressly and unambiguously places a federal association's right to include and enforce a due-on-sale provision on a par with the right of any other party to so contract for such a term. The purpose of the regulation is not to vest federal associations with any extraordinary right to the inclusion

4. Apparently defendants' notion of *freedom* of contract perverts the traditional concept of parties of equal strength *freely* exchanging concessions to arrive at an agreement on mutually beneficial terms, and replaces that with the concept of one stronger party *freely* dictating terms unilaterally beneficial to itself.

of a due-on-sale clause. The regulation vests a federal association with no rights, whatsoever, but merely clarifies that, with the exception of the new restrictions placed on a federal association in subparagraph (g), it "continues to have the power" to bargain, as any otherwise unrestricted party, for a due-on-sale clause in its loan contract.

The gist of the regulatory scheme is manifestly to provide further protection to borrowers by adding the restrictions listed in subparagraph (g). It would be absurd to contend that the aim of paragraph (f) was to completely strip the borrower of any other protection to which he or she might be entitled. The very fact that subparagraph (g) places restrictions on its use provides compelling evidence that the due-on-sale clause is deemed to be a dangerous provision, the use of which warrants careful scrutiny. Consequently, assuming that the subject federal regulation is the applicable law in this case, it is only reasonable to presume that a federal lender is, nevertheless, subject to those external restrictions designed to protect a borrower to which any other lender is subject.

B. THE CONTRACTUAL PROVISION RELIED UPON BY DEFENDANTS IS ADHESIVE AND NOT ENFORCEABLE UNDER GENERAL PRINCIPLES OF CONTRACT LAW; THE ABSENCE OF MEANINGFUL CONSENT TO THE TERMS OF THE SUBJECT INSTRUMENT BY THE BORROWERS VITIATES THE EXISTENCE OF A TRUE CONTRACT, WHICH IS A CONDITION

PRECEDENT TO THE APPLICABILITY OF THE SUBJECT FEDERAL REGULATION, TAKING THIS MATTER OUTSIDE THE AMBIT OF THAT REGULATION.

The federal regulation relied upon by defendants provides that the inclusion of the due-on-sale clause in a federal association's loan instruments is a matter of *contract* and that the exercise of that clause

> "... shall be governed exclusively by the terms of the contract between the association and the borrower, and all rights and remedies of the association and borrower thereto shall be fixed and governed by said contract." 12 C.F.R. § 545.8-3 (f).

There is nothing in the language of the regulation, nor in the language of HOLA, nor in the body of federal legislation, nor in the federal Constitution, and nothing has been presented by any defendant, and no defendant has attempted to argue, that the term *contract* as used in the regulation is used in any sense other than its traditional sense, i.e.

"...an *agreement* to do or not to do a certain thing."
Civil Code §1549 (Emphasis added.)

The elements essential to the existence of a contract are 1) Parties capable of contracting, 2) their *consent*, 3) a lawful object, and 4) sufficient consideration. Civil Code § 1550; see Rest., Contracts §19. In the instant case, it is the failure of the borrowers to have knowingly and voluntarily *consented* to the due-on-sale provision of the federal

association's loan instrument that stays the Court of Appeal's authority to enforce the literal terms of the agreement as per the federal regulation. For, until there *is* a valid contract between the association and the borrower, the subject federal regulation is not applicable. A construction of the regulation which requires enforcement of the contract regardless of equitable defenses thereto would violate the parties' constitutional rights to freedom of contract and to due process, and would therefore be improper. See *Shealor v. Lodi*, 23 Cal. 2d 647, 653 (1944).

In *Graham v. Scissor-Tail, Inc.*, 28 Cal. 3d 807, 623 P. 2d 165, 171 Cal. Rptr. 604 (1981), the Supreme Court of California, in holding that a compulsory arbitration clause contained in two standard form musicians' union contracts was unenforceable, treated the issue of voluntary consent and adhesion contracts under circumstances which parallel the case at bar in several respects.

Graham was a promoter and producer of musical concerts who entered into the two contracts with defendant Scissor-Tail to promote two outdoor concerts. Defendant was a member of the American Federation of Musicians (AF of M) and required plaintiff to execute AF of M's standard form contracts, which included compulsory arbitration provisions. A dispute as to losses incurred by the concerts ensued and plaintiff, a non-union member, was compelled by the lower court to submit to arbitration by a union board. The court found that the union was an interested party and that an arbitration

proceeding by an interested party would "render (a) fair and reasonable decision . . . a virtual impossibility". *Id.*, 28 Cal. 3d at 827.

The court found that the AF of M contract was adhesive and then proceeded to determine under what conditions an adhesion contract will not be strictly enforced:

> "Generally speaking, there are two judicially imposed limitations on the enforcement of adhesion contracts or provisions thereof. The first is that such a contract or provision which does not fall within the reasonable expectations of the weaker or 'adhering' party will not not be enforced against him. (Citations.)The second - a principal of equity applicable to all contracts generally - is that a contract or provision, even if consistent with the reasonable expectations of the parties, will be denied enforcement if, considered in its context, it is unduly oppressive or 'unconscionable'.(Citation)." Id., 28 Cal. 3d at 820.

Graham cites *Madden v. Kaiser Foundation Hospitals*, 17 Cal. 3d 699, 131 Cal. Rptr. 882 (1976), where the Supreme Court of California observed that

> "(i)n many cases of adhesion contracts, the weaker party lacks not only the opportunity to bargain but also any realistic opportunity to look elsewhere for a more favorable contract; he must either adhere to the agreement or forego the needed service. *Id.*, 17 Cal. 3d at 711.

In the case at bar, the Court may take judicial notice of the fact that a prospective home purchaser has little economic choice but to deal with an institutional lender. The Court may also take judicial notice of the fact that lenders generally present a united front, offering substantially identical home-loan terms, so that, in effect, the borrower not only lacks the opportunity to bargain but also any realistic opportunity to look elsewhere for a more favorable contract.

It is clear from the record in this case that there is no parity of bargaining strength between the weaker borrower and the stronger federal lender, and that, at the time the subject loan was made, the borrower had no "realistic opportunity to look elsewhere for a more favorable contract." Consequently, even if the Court of Appeal had applied the subject federal regulation, it would have been necessary to examine defendants' use of the due-on-sale clause to assure fundamental fairness to the weaker party. The Court would not have blindly enforced the terms of the written contract as defendants urge.[5]

5. Since the introduction of the concept of adhesion contracts to American jurisprudence, courts have universally refused to blindly enforce the strict terms of such instruments where they impose an inherent unfairness on the weaker party.

See generally *Henningsen v. Bloomfield Motors, Inc.*, 32 N.J. 358, 161 A. 2d 69 (1959); *Standard Oil Company of California v. Perkins*, 347 Fed. 2d 379 (9th Cir. 1965); *Chandler v. Aero Mayflower Transit Co.*, 374 Fed. 2d 129 (4th Cir. 1967); *Neal v. State Farm Ins. Cos.*, 188 Cal. App. 2d 690, 10 Cal. Rptr. 781 (1961); *USA Chem., Inc. v. Lewis*, 557 S.W. 2d 15 (KCD 1977); *Cutler Corp. v. Latshaw*, 347 Pa. 1, 97 A. 2d 234 (1953); *Star Finance Corporation v. McGee*, 27 Ill. App. 3d 421, 326 N.E. 2d 518 (1975); *St. John's Episcopa Hospital v. McAdoo*, 94 Misc. 2d 967, 405 N.Y.S. 2d 935.

Defendants in this action unabashedly claim that exercise of the clause has nothing to do with the impairment of the security for the individual loan, and has nothing to do with the particular contract or borrower; but that exercise of the clause relates to *defendants' ability to* maintain loan portfolios at current interest rates.[6] The Supreme Court of California has held that such is an improper use of the due-on-sale clause and

> "... that it would be unjust to place the burden of the lender's mistaken economic projections on property owners exercising their right to freely alienate their property through the automatic enforcement of a due-on-sale clause by a lender." *Wellenkamp, supra,* at 952-3.[7]

Moreover, even if the due-on-sale clause can be justified to maintain loan portfolios in order to advance the purpose of HOLA (a questionable proposition), the

6. While the maintenance of viable loan portfolios might be a legitimate concern of the federal lenders, it is, nevertheless, incidental to the main purpose of HOLA, which is to provide suitable financing for home purchasers. Where efforts to maintain loan portfolios severely restrict the rights of the home purchasers, and price many potential purchasers of used homes out of the market, the legitimacy of the federal lenders' claim to the protection of HOLA becomes suspect.

7. *Wellenkamp* itself appears to rely heavily on the theory of adhesion contracts. See Gauntlett, *Wellenkamp v. Bank of America: Invalidation of Automatically Enforceable Due-on-Sale Clauses,* 16 Calif. L. Rev. 886 (1979).

right of the federal lender to impose the clause on a borrower at the lender's option (a borrower is in no position to bargain otherwise), in order to advance HOLA's purpose, constitutes an improper taking by a private party and violates fundamental notions of due process. Cf. *Adams v. Egley,* 344 F. Supp. 614 (s.d. Cal. 1972); *Thompson v. Consolidated Gas Utilities Corp.,* 300 U.S. 55 (1937); *Fuentes v. Shevin,* 407 U.S. 67 (1971). It follows that the automatic enforcement of the due-on-sale clause in this case fails to assure fundamental fairness to plaintiffs, thereby rendering the clause unenforceable under universal principles of contract law.

Interestingly, a preemption argument is raised in *Graham,* but the court held that preemption is immaterial where there is no conflict between state and federal law. 28 Cal. 3d at 830-831. In the case before the bar, the federal law advanced by defendants contemplates the existence of a contract - *a true consensual agreement* - as a condition precedent to its applicability. Should the Court find a true consensual agreement between the borrower and lender, only then should it struggle with the issue of preemption. However, it would appear that, under *Graham* and authorities cited therein, there is no true contract involved in this case (the element of *consent* is absent) and, by its very terms, the federal regulation is not

applicable.[8] Consequently, there is no point of conflict between state and federal law, and the issue of preemption is immaterial and moot.

III

SUMMARY

Defendants have calculatedly oversimplified the issue in this case as one of preemption, federal law prevailing over state law. The characterization is based on at least four false assumptions: 1) that the Supreme Court of California decision in *Wellenkamp* constitutes *state law* as that term is applied in preemption cases, 2) that the subject federal regulation is necessary to maintain nationwide uniformity in the practices of federal lenders, 3) that the constitutional issues all fall on the side of defendants, and 4) that the subject federal regulation allows the automatic enforcement of the due-on-sale clause. However, it is not necessary for the Court to reach the issue of preemption, in that it is moot.

8. The Court in *Graham* found that the federal law invoked in that case contemplated the existence of a true contract - not an illusory arbitration provision. *Graham* declined to find "that the substantive federal law of collective bargaining agreements requires any result different from that which we have reached." 28 Cal. 3d at 830. Appellees herein urge that the substantive federal law invoked by appellants contemplates the existence of a true contract - not an adhesive provision which effectively "takes" equity from the purchaser without compensation; and that the substantive federal law would not require any decision other than that reached by the Court of Appeal.

It is clear that the contract in this matter is adhesive and that the terms were accepted by the borrowers only under conditions of economic coercion and duress. By its very terms, the subject federal regulation embraced by defendants requires a valid contract as a condition precedent to its applicability. Here, lacking true *consent* of the borrowers, that condition fails. Therefore the federal law is inapplicable and the due-on-sale clause may not be enforced if it is fundamentally unfair to the weaker party, here, the borrower. Not only has the Supreme Court of California found the automatic enforcement of the clause to be fundamentally unfair; but also, 12 C.F.R. § 545.8-3 (f) and (g), in absolutely prohibiting the use of the clause under certain circumstances, including involuntary transfers,[9] and in allowing its use otherwise only when a borrower has agreed in a contract to accept the clause, raises a strong inference, if not a presumption,[10] that the

9. It might be effectively argued that the borrower's involuntary acceptance of the clause in the adhesive instruments herein, brings this case within the ambit of 12 C.F.R. § 545.8-3 (g), which prohibits use of the clause in the event, *inter alia,* of an involuntary transfer of the property. There seems to be no logical distinction between that situation and a situation where submission to the inclusion of the clause itself was involuntary.

10. It might also be argued that, assuming the federal regulatory scheme was designed to encompass every possible contingency, the federal regulation conditioning the enforceability of the due-on-sale clause exclusively on the terms of the contract between the borrower and lender necessarily includes an implication that a finding that no valid contract exists raises a conclusive presumption that the clause is unenforceable.

clause is fundamentally unfair, but enforceable only under Federal law as well as State law upon voluntary waiver by the borrower. Accordingly, the clause herein is unenforceable.

DATED: March 5, 1982

Respectfully submitted,
JOHN W. DUMAS
Attorney for Appellees.

DECLARATION OF SERVICE

I, the undersigned, say:

I am a citizen of the United States and a resident of Orange County, California; I am over the age of eighteen years and not a party to the within entitled action; my business address is 611 Civic Center Drive West, Suite 201, Santa Ana, California 92701.

On I served the within by placing true copies thereof enclosed in sealed envelopes with postage thereon fully prepaid, in the United States mail at Santa Ana, California, addressed as follows:

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California Court of Appeal
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I declare under penalty of perjury that the foregoing is true and correct.

EXECUTED on at Santa Ana, California.

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